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PRESIDENT'S PAGE

Recently I have heard several comments referring to the "average" man or the "average" of whatever group happened to be the subject of the conversation. It is apparently assumed that there exists an average person in every group. This has prompted me to speculate as to whether people might imagine there is a person who would be the average member of our Illinois Society of Certified Public Accountants.

The question follows, "Who would seek out the *average* CPA?"

The answer might be that only a statistician would be interested in the person who would have all of the attributes of a computed "average." An accountant would, of course, prefer to be sought after by a potential client or employer. We, therefore, are all interested in developing attributes which place us in a class which gives us standing as individuals rather than as statistics.

The engagements accepted by a sole practitioner CPA and the responsibilities placed upon a member of an accounting organization, large or small, call for something more than average performance with respect to the particular activities to which the accountant is asked to direct his attention.

Not all members of the accounting profession, and not even all of the members of The Illinois Society of Certified Public Accountants, will attain the maximum proficiency in every aspect of accounting. The secret of success for the accountant, as is true with respect to any professional man, is that there are one or more specific areas in which he is able to make a contribution and perform work far above the average level. Success comes, therefore, when a man develops a proficiency in serving the business community as regards whatever engagements he undertakes. These tasks may embrace the auditing of relatively small businesses, the auditing of the accounts of the larger corporations, assisting the individual businessman or the large corporations in improving their record keeping technique, assisting business in a proper determination of tax obligations, and any number of other activities.

Superior performance, or even performance at or just slightly above the level of "average," is a result of continuous effort for improvement and study.

At the outset of the fiscal year for which I will be serving as President, it seems appropriate to state that the over-all goals adopted by the Directors of the Society for the current year call for, first, continued emphasis

upon the necessity for adherence to the highest ethical and technical standards and, second, further development of a program to create keener understanding of the significance of the CPA certificate by, among others, CPAs who need to be encouraged to continue their professional development.

The objectives of The Illinois Society of Certified Public Accountants include the rendering of assistance to members in obtaining knowledge and developing abilities in such manner that there will be outstanding performance. If the individual member will take advantage of the meetings which are planned and carefully study the printed matter received through the mails, he will find himself doing his work better, obtaining increased confidence, and attaining a position as an accountant in which he is recognized as above average—whatever "average" may mean with regard to his particular activities.

Raymond A. Hoffman

PROFESSIONAL ACCOUNTING ANSWERS ITS CHALLENGE

By John W. Queenan

Future in General

When I speak to you today about the future of our economy and of our profession, and of the ability of both to meet their challenges, I must admit that I speak as an optimist. Practically all of the tested economic indicators not only point toward a strong business situation in the next few years, but in addition presage a broad economic expansion of startling proportions. The onward surge of the projected population growth of our nation, and of our increasing productivity per capita, makes any forecast beyond the next ten years a rather fuzzy one.

Our recession on a national scale is behind us, but there are still pockets in our economy where the recovery has not shown itself, neighboring Michigan being an outstanding example. This is not surprising, however, when we consider that such an eminent authority as Martin R. Gainsbrugh, Chief Economist of the National Industrial Conference Board, tells us that the downward trend from July, 1957 to April, 1958 was the most severe nine-month decline in the history of our country. So, although the recession on a national basis was short-lived, it was violently severe, and some of our industries were hit so hard that they are still groggy. But the evidence is unmistakable that the economy as a whole has recovered and is moving at a very rapid pace.

When I was a boy in Aurora, just a few miles from here, construction of the St. Lawrence Seaway was still in the dream stage. Now after years of debate which preceded its final approval in 1954 by both the Canadian Parliament and our Congress, the reality of a channel with a minimum depth of 27 feet, which will be ours, opening to ocean-going ships this entire great area of inland seas, brings prospects of expanded benefits and economy which at the present moment I believe are incalculable. Chicago, I think, is certain to get an important part of Seaway traffic, thanks to its industry and to the natural advantages of its geographical position which gives access to vast sections of our country served through its large rail and truck connections. There will almost certainly be a greater total commercial life and industrial power for the continent as a whole. The Great Lakes will have become the fourth seacoast of the United States.

Add to these immediate national changes those of the near future hav-

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ing an international impact—missiles, satellites, and space travel, to mention only a few of the more glamorous—and you see a world on the verge of vast scientific and industrial developments which may well change our way of life and, indeed, our whole outlook as it relates to our fellowman.

What, then, will be the impact of all these factors on our progress as a professional group? For one thing, they certainly will place upon our profession additional obligations and responsibilities and—a point we should not overlook—additional opportunities. There will be not only massive growth of population but also a broad growth of our profession. If we merely continue to move along as we have been doing, the volume of our work and the number of certified public accountants could be expected to increase just as a matter of arithmetic in harmony with our expanded national statistics. But the more probable result to look for is that the demand for our services will increase much more rapidly than in direct relation to the increases in the gross national product and in our population. The certified public accountant has contributed importantly to the rapid growth of the industrial economy. He will not be content with what he has already achieved, I am sure. With new fields of knowledge to master, the accounting profession is being continually called on to improve the competence of its members—to do better, today and in the future, the things we now profess to be able to do well; to attain a degree of skill in new areas compatible with existing areas of expertness.

The experience and professional knowledge of trained accountants have never had greater scope and the expanse of the future should prove to be infinitely more dynamic than the past.

Professional Status of Accounting

Accountancy has made such great progress in achieving acceptance by the public that it should rank as a genuine profession rather than as a specialized vocation, but reservations still exist in some quarters. We need to move forward on a broader front and to take steps to consolidate our gains.

Professional standing is not attained without acceptance of responsibility. The heavier the responsibility, the loftier the profession. There are a number of marks identifying a profession, such as adherence to a code of conduct, self-discipline, high standards of education, and significant public service—but the quality that really sets apart the professional endeavor is the presence of significant responsibility and the willingness to accept it.

Our Challenge

The very progress already made in achieving acceptance of our profession and the outlook for the future challenge us to meet our responsibilities and, by eliminating weak spots, to strengthen the profession internally, broaden our field of service to clients, and sharpen our sense of responsibility to the public. No single discussion can pretend to cover with any degree of completeness a subject as vast as this. My remarks, therefore, will be confined to the more general and, in the long range, more basic matters that face our profession.

Attracting, Developing, and Retaining Outstanding Talent

The demands of the future will require many more trained accountants

with a higher level of education than at present. The vitality of any profession depends in substantial measure on a steady influx of young men of character and professional promise. The future of the accounting profession would seem to require an ever-increasing stream of such young men.

This is a serious situation. What should the profession do to attract a larger number of the right kind of individuals? Should we change the educational requirements? What kind of experience should a man have before being accepted as a CPA?

When a person decides to become an accountant he is accepting the responsibilities of the profession. He is also assuming certain social, ethical, and legal obligations associated with the unique character of our work and its relation to the public. The crux of the matter, therefore, is attracting the right kind of people, who are able and willing to acknowledge these larger aspects.

We need to consider further the ways in which promising high school students may be channeled into accounting. We have done very little as a profession in the way of attracting outstanding high school students. Our profession is too young to have the traditions of law and medicine which have a strong public service appeal. Somehow, we must find a way of interpreting the nature and significance of accounting to young minds.

Education

We must refine the present method of accounting instruction. We must set new patterns in professional accounting education. We must develop the professional teaching of accountancy. We must devote more professional leadership to establishing more effectual liaison with the schools and their correlated activities—professional and educational. We must provide financial assistance that will lead to improved educational background for those entering the profession. The colleges and universities are in a ferment of new ideas and new spirit and the profession must do better than keep pace. It must lead.

The need for re-examining the educational and experience requirements for the CPA has long been recognized by many leaders of the profession, and important phases of the problem were thoroughly reviewed in a realistic report published three years ago by the Commission on Standards of Education and Experience for Certified Public Accountants. The principal recommendations concerned, first, emphasis to be placed on formal academic training; second, the part of the training of a CPA to be acquired through practical experience; and third, the timing of that experience in relation to the CPA examination. At this year's spring meeting of Council of the American Institute, there was adopted a definite policy with respect to education and experience requirements for CPAs, embodying the Commission's recommendations. The policy recommends a baccalaureate degree and eventually a fifth year of collegiate study for CPA candidates, but would retain the requirement of some accounting experience before the certificate is awarded.

Just as considerable time elapsed before uniformity in the CPA examination could be brought about, it may be a long time before differing opinions regarding these points are resolved on a national basis. But I am certain there will be complete unanimity about the kind of end product

we want. We will want to develop and support those policies in education and practice that will prove more emphatically to the public that the CPA certificate is an evidence of superior technical skill and professional responsibility.

We will want to establish policies that will add emphasis to the professional standing of accountancy.

We will want to support and strengthen two of the mainstays of the CPA—objectivity and independence.

The achievement of such an end product will require patience, the application of tough thinking, and much common sense.

It represents a challenge that is worth the serious attention of each one of us.

Continuing Education and Self-Development

All of our challenges, when reduced to their common denominator, are met through a broad program to increase the competence and stature of CPAs, in areas both of formal education and of continuing education and self-development.

It is good to know that this Illinois Society is discussing the question, "Is Your Professional Development Continuing?" An affirmative answer to this question is essential if we are to face up to all our challenges and opportunities on a broad front.

The American Institute, through its new Division of Professional Development, is taking the lead in meeting this important objective. Your Illinois Society, like CPA societies of many other states, has not only responded to the call issued by our national body but has itself initiated many important steps.

We as individuals have a solemn obligation to develop ourselves to the fullest extent. We are all gifted in various ways in varying degrees. Our responsibility is to utilize these talents in the most effective way. Simply stated, as each year goes by, we must become better accountants. Each must accept the hard disciplines of continuing education, the rigors of creative thinking, and the responsibilities of professional activities, not only in our own personal interest but in the interest of society as a whole.

Accounting Principles—United States

We are fortunate that in accounting there are the room and the need for the exercise of experienced judgment, intelligent thinking, and imagination. Out of these ingredients are bred new ideas for improvement, advancement, and increased efficiency and economy. This presents an imposing challenge to the profession. It is up to us, as a profession, to contribute our share of such new ideas.

Considerable progress has been made over the past twenty years in the development of accounting principles, beginning with the study which was the basis of the Statement of Accounting Principles by Sanders, Hatfield, and Moore published in 1938. The Accounting Procedure Committee of the American Institute, which was established in the same year, has accomplished much in promoting the development and recognition of accounting principles, and in advancing their observance perhaps to a greater extent than anywhere else in the world.

While we have made marked progress in developing a set of accounting principles that have become in-

valuable in clarifying and improving corporate accounting, I fear we have not made similar progress in achieving greater uniformity in applying these principles. This is one of the chief criticisms directed at accountants today. Comparisons of companies, it is contended, are difficult because of the apparent lack of uniformity in applying accounting principles. We should strive to narrow the differences in application wherever we feel that greater uniformity is possible and desirable. In situations where uniformity is not practicable, our aim should be to gain a better understanding of the problems involved through educational efforts in the field.

The profession must continuously seek to widen public understanding of the fact that operating results and financial position reflect not unimportantly the attitude and philosophy of company management and that net income is not just a figure produced by a calculating machine.

We also need to inform the public that apparent differences in applying accounting principles frequently are the result of a "going concern" approach in one instance, a "liquidating" approach in another, and perhaps a mixture in others.

While I believe that we can make more progress in achieving greater uniformity in applying accounting principles, I am also convinced that there is a limit to uniform application. The free enterprise system and, indeed, constructive and informative accounting cannot exist in a strait jacket. The best proof of this is our experience with charts of accounts and accounting procedures promulgated by regulatory bodies for an industry. The profession must, by assuming responsibility in this area, demonstrate the deadly inertia produced by such restraints.

The current program on the part of the AICPA in connection with research in accounting deserves our full support. As approved by Council at its spring meeting, a director of accounting research and members of a new research staff will be selected as soon as possible. This staff will function in cooperation with an Accounting Principles Board, which is composed of representatives of industry and the teaching profession as well as members in practice. This constitutes a new approach to the means by which accounting research should be undertaken, accounting principles promulgated, and adherence to them obtained. In years to come, I am certain we will look back to this event as one of the landmarks in the history of our professional development.

Accounting Principles—International

On a broader front, we face too the challenge of lessening the divergences that exist in accounting principles and in their application on a global basis. One need do no more than read the financial pages of our daily newspapers to realize the impact of international trade and foreign investment on our economy.

Despite the ever-growing interrelationship of the nations of the world in international trade and finance and the need for informative financial information between the parties, there remain many differences in accounting practice among various countries. Codes of accounting conventions and authoritative groups to define and promote their application do not exist except in English-speaking countries and in Germany and Holland. Fixed assets are frequently

revalued to recognize currency devaluation. Only in the United States is the Lifo valuation of inventory recognized. In Great Britain, on the other hand, direct costing is an accepted accounting convention. Income tax liabilities are often not accrued at the end of the period to which they apply, but are expensed in the next year when paid. Consolidated financial statements are unknown in some areas. Stock dividends are treated as income in some instances.

These are but a few of the differences that exist in practice throughout the world. Similarly, auditing standards, disclosure standards, attitudes toward independence, and report terminology differ considerably. There is no doubt that we have our hands full in reducing the number of variations now existent in practices and standards in our own country, but I believe concurrent attention should be given to this over-all problem of accomplishing a greater conformity among nations in their treatment of similar accounting matters. Meetings of the International Congress on Accounting such as those held in London in 1952 and in Amsterdam in 1957, and the one scheduled for New York in 1962, do much to emphasize the differences that exist and to provide the groundwork for attaining greater uniformity.

Interdependence of Members of the Profession

Perhaps the greatest need in the present stage of development of our profession is a more widespread recognition of the interdependence of its members—of the fact that the effect of the actions of each member on the prestige and character of the profession is either positive or negative. It is seldom neutral. Each accountant has a duty to his contemporaries that pertains to such matters as ethics, conduct, and furtherance of the profession's affairs. Laxity in the discharge of duties concerning ethics and competence may take away from what the profession has attained and from what the accountant has won at great effort. None of us can expect to gain in the long run by making temporary capital at the expense of the other.

Just as the conduct and work of each certified public accountant affects the profession as a whole, so too is the standing of our profession tinged with the actions of non-certified accountants. As much as we may wish to disassociate our profession from non-certified accountants, the fact remains that we have not successfully done so in the public mind. We have a responsibility, therefore, reluctant though we may be to accept it, not only to educate the public as to differences among classes of accountants but to do everything possible to bring about regulation of all public accountants and to assist them in raising their level of competence and performance. If we are to convince the public that the certified public accountant belongs in the professional sphere and that the non-certified accountant operates in the area of the technician, our performance must merit that conclusion. There is no lack of opportunity for all CPAs to use their talents to the full extent of their professional competence. The time has come, I feel, for CPAs to leave such work as bookkeeping for the technician and to concentrate on fuller use of their professional training.

Over the years various members of small and medium-sized accounting firms have expressed concern over

their own problem of survival, particularly where the location of their practice brings them into continuing association with national firms. Mergers of various accounting firms have raised questions as to whether it is inevitable that all work be concentrated in a few large firms. First of all, I should like to emphasize not only that there is room for both types of practitioner, but also that our economy today *demands* that we have small and large firms of certified public accountants. And this is just as true in Chicago as it is in New York City, or Houston, or Los Angeles, or any other city where business is being done by giant international corporations, medium-sized corporations or partnerships, or sole proprietorships.

A word you will hear many more times in this meeting is *service*. Service is the key to progress. It symbolizes that the interest of the public we serve must be our first consideration at all times. If each of us concentrates on following this test of action, other practitioners, including national firms, become not competitors but contemporaries. The result of the striving of each of us to raise our own professional stature will not only bring to each as much work as he can competently handle, but also will serve to engender in the public as a whole a greater respect for all practitioners, large and small.

In the interest of serving clients better or of insuring continuity of such service, many an individual practitioner or small firm has merged his practice with another comparable group. There are obvious advantages in considering such a serious move, but, unfortunately, in many cases such moves are matters of expediency because of neglect of certain essentials in the past. The need for merger can be avoided by meeting the demand for special services and by making adequate provision for continuity of the firm. In a three-partner firm, for example, one partner might concentrate entirely on tax matters. The second could train himself to become expert in the field of management advisory services. The third partner could handle audits and would be responsible for the general administration of the practice. This does not mean that each partner would devote his entire time to his specialty only, nor should he divorce himself from the other phases of the practice. That survival of a firm as a continuing entity is contingent upon due attention being given to two principal vital areas seems quite clear. First, the firm must steadfastly maintain its competence to serve its clients by continuous effort at improving its techniques, its staff, its ethics, and its reputation for top-level work; and second, the partners must make adequate provision for continuing their firm by developing staff members to the point where they can be admitted as partners and by providing for the orderly retirement of existing partners. If these conditions are met, there is no reason why any firm should not perpetuate itself.

In our own organization we have had a number of mergers with smaller accounting firms over the years, and other discussions that did not materialize in a tangible way. It may surprise you to know that over 95 per cent of these mergers and merger discussions were initiated by the other parties, the smaller firms. In many cases they come to us because they had not included among their objectives in their early years that of a planned continuation of

their firm, with the necessary elements of planned partnership development, retirement, and succession. This aspect of accounting practice—the ability to look ahead, to formulate future plans, and to act upon them on schedule—is a highly significant management factor in all public accounting organizations. The administration and long-range planning of an accounting practice must not be a haphazard duty relegated to those moments when the partners think they will have the time to devote to it.

The very strength and vitality of our profession require breadth in its composition by the participation of firms of all sizes, from sole practitioners to large national firms, and depth in the strength of organization and competence of those firms.

Public Expression

An important challenge to the certified public accountant is the duty he owes society and the community in which he lives. This duty includes performing public service of many kinds and taking an active part in the public forum, particularly when the accountant's competence fits him well to discuss the issues. Failure of the individual accountant to accept this duty may block his professional progress, and failure of many to accept it may deter the advance of the profession. The penalty for neglect of this duty is stunted growth.

I think it is fair to say, however, that some of the other professions, such as law and medicine, sometimes do more than our own in expressing a sense of obligation to the public. The public's appraisal of our profession will most certainly be measured in terms of the broad social objectives of other professions whose members contribute to general community improvement. We should endeavor to participate with them and other groups as much as possible in solving problems of public interest.

If people recognize that CPAs, with their special skills and techniques, are concerned with the common good, the public will inevitably conclude that accountancy, too, works for the general welfare. These are the characteristics of a profession that are most apt to influence public opinion.

We must strive at all times to create a greater reservoir of public knowledge about ourselves.

Acquainting the Public with What We Do

At this point may I expand this theme with a few brief thoughts. My basic idea is this: need is urgent for better public understanding of the certified public accountant, what he does, and why he is important to our society. It is not difficult to understand the first reaction of many CPAs that the public be "educated" by means of a public relations campaign sponsored by their professional societies.

This is a responsibility these groups have met, and are meeting. We are all familiar with the expansion of this theme by means of pamphlets, trade-press articles, movies, radio, and television programs.

This approach, if it is to culminate effectually, must be sharpened by individual effort, and that is where you and I enter the scene. When we talk to clients in the terms of the client's problems, and how accounting fits in, we are helping in this effort. We can do the same in conversation with friends about careers for their children, with neighbors about their tax

problems, with bankers about credit problems, and with lawyers in a wide variety of fields. In the course of such talks it should be easy to indicate the technical and ethical standards of CPAs and the type of work they do. Many people associate the activities of a CPA with examining large sheafs of paper or with adding machines and arithmetic; we must point up the importance of such factors as analysis, independent evidence, observation, and the result of all of these—the exercise of professional judgment.

Every day each of us makes certain impressions on individual citizens—what we say, what we do, how we live, the fees we charge, how independent we seem, how well informed we are—all of these result in a sum total, the public image of the CPA. Meeting the challenge in this all-important area of acquainting the public with what we do is a continuing responsibility for us all.

Inflation

Inflation, which challenges our dollar, is a basic concern to everyone. I do not plan to devote much time to this important subject, chiefly because it has been much discussed by many groups in many places, but on the other hand, I do not wish to ignore it in any discussion of challenges to accountants. This is one we must meet, and meet squarely. Fiscal stability can be achieved through hard work, self-discipline, and determination, qualities which have made America what it is today. Our specific part in this pattern lies in our ability to improve accounting controls so that maximum cost savings and productivity growth are made a matter of record, for along with the recording and measurement of these factors comes an incentive on the part of industrial management to strive for even further progress in this direction. I am thinking particularly of the part we can play in seeing that cost variations are spelled out in such a specific way that the factory-floor foreman, for example, gets prompt credit or blame for a favorable or an unfavorable performance. The battle against inflation has its own firing line, I am convinced, and it is there that we must fight to hold the line.

Conclusion

Expansion of our economy, scientific developments, mass growth of the population and of our profession will present many problems and challenges. But it is on the new frontiers that progress is born. Out of necessities arising from environment the pulley was invented, later making possible the erection of great buildings and monuments. Out of the necessity to contend for professional recognition came the perception that in service and responsibility lay the keys to that end, and in being guided by these ideals we have seen our profession achieve stature. If we face our challenges forthrightly we shall see that stature enhanced—standing, so to speak, as a monument to our public service.

THE IMAGE OF PROFESSIONALISM

By Charles P. Rockwood

We are witnessing a scramble among new professions for recognition. The pace is quickening, and public relations is in the midst of it. Time was when the professions were thought to consist of law, medicine, and the ministry, teaching and military arms. Now there are others, like accounting, architecture and engineering, and there are many semi- or quasi-professions: insurance, advertising, banking, journalism, the fine arts and pharmacy come readily to mind.

Professionalism is also claimed by morticians, beauticians, watchmakers, florists, photographers, plumbers, and also by egg graders, dog trainers, well diggers and yacht salesmen!

Fostered Specialization

This is not necessarily bad. All things considered, it is probably good. Modern society has fostered specialization to the general betterment of the more advanced economies. More people are better educated than they used to be and there is more training to be had in a wider variety of vocations. It has been noted by Professor Walter Gellhorn that nurses and other "semi-professionals" today must master a larger and more useful body of knowledge for the care of the sick than the *entire medical knowledge of a century ago*. People like to distinguish their work from mere "jobs." The public relations problem posed by the trend is this: the more vocations that strive for professional status and take unto themselves professional trappings, the harder it becomes to distinguish them from other jobs. The image of professionalism gets blurred.

Running through all the reasons for this movement is the desire for public *recognition* as a profession. In the end, it is *public opinion* which bestows the coveted mantle. When it is assumed otherwise, it is ill-fitting and the wearer looks comical. So, in many respects, the attainment of professional status is a public relations problem.

What Can We Do?

What can public relations do about it? Can public relations live up to expectations—for certainly the aspiring vocations are using it hopefully, and the older, established professions are too, lest the public forget. Since the goal is the achievement of public recognition, let us see what it is that most pepole think of as professional. What is the public's image of professionalism? And, if the image is

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being blurred by the wholesale scramble for it, how can it be sharpened?

Five generally recognized attributes of the image can be identified, each to be established clearly by all who would apply public relations techniques to enhancing professional status.

Professions Are Individuals

Professionalism is a highly individual quality to be found in individual people. It is true that professional men also associate for a variety of important reasons, and that associating is essential to the professions. But it is not simply organizing that makes men professional; it is the individual who professes.

For example, in deciding whether to regard certified public accountants as professionals, the public makes up its mind by watching CPAs as people. The collective decision is made on Main Street, across the desk of every client, in church basements and PTA meetings and on the 18th and 19th holes of the golf course. It is for this reason that, while public relations solutions can be approached through organizations, the closer the application is to the individual, the nearer it is to success. Consequently the problem must be defined and solutions prescribed in terms that professional people can understand and remember. It is the task of public relations to persuade them to be good ambassadors for their profession as a whole. They must never be allowed to forget that their individual fortunes rise or fall with the group's, and that they each have a personal responsibility for the group image.

This manifestation of professional qualities by individuals makes it easier to demonstrate professionalism with public relations techniques, because generalizations can be avoided. Professional attributes can best be revealed in terms of actions which people can understand and which make attractive copy: this professional man was educated at a certain university and holds certain degrees. He travels to a distant campus to deliver a paper or attend a seminar. His subject was professional ethics, and so on.

A Growing Body of Learning

Professionalism supposes a body of learning and knowledge to be mastered. It is the job of public relations to reveal it—a never-ending task calling for ingenuity not only on the part of the public relations specialist but by the professional man himself. Ceremonies can be arranged to recognize the passing of examinations and attainment of academic degrees. The granting of licenses to practice is harder to celebrate, but it is by no means impossible. Dinners can be given in honor of recipients, addresses delivered, photographs taken of the awarding of the certificate.

Sharing of Knowledge

It is characteristic of the professional man that he shares his knowledge, his discoveries and opinions with his fellow practitioners. Professionalism and trade secrets don't mix. The public stands to gain by this unselfish circulation of wisdom and technique, and the profession is thereby distinguished from more competitive trades. An appropriate way of attracting attention to individual contributions to the body of knowledge is by the awarding of medals. The authorship of books and articles can be given public notice.

So can professional meetings which demonstrate the willingness of practitioners to travel at their own time and expense, tax deductions notwithstanding, to absorb more skill and understanding for the benefit of their clients as well as to enhance their own prestige. The profession's concerns can be revealed to the public through press reports of the list of subjects for discussion.

A further characteristic of professional knowledge is that it is always growing. We have extra confidence in the practitioner who keeps up with the current literature. His participation in continuing education programs and seminars makes news.

A professional man must be more than an expert. His learning must be broad, encompassing a wide culture and general understanding of affairs. This permits him always to relate his specialty to the whole and to see significance to society in what he does. He then naturally acts like a significant person and is accorded deference outside his chosen fragment of human activity. He should be urged on public relations grounds to speak out on issues of public consequence in which his specialty has some bearing.

Concern for the Common Good

Professions are expected to show a concern for the public welfare. This is an outgrowth of the significance of their specialty to society, and it can be expressed visibly for public relations purposes. For example, lawyers know that the need for their skills as advocates arises only in a lawful society, and they consequently promote wide respect for the law through such devices as the new "Law Day—USA." Doctors should show an interest in a high level of public health, for without it their attention would have to be restricted to a much lower order of medicine than is generally practiced today. Their support and staffing of public and private agencies and organizations in this field should be publicized. Certified public accountants would find less demand for audits and accounting work in an elementary economy lacking a public acceptance of high standards of disclosure and accountability. So they promote business ethics and fair representations in financial reporting.

Professional men also express their concern for the common weal in areas outside their specialty. Many communities are accustomed to their leadership in all manner of civic, cultural, charitable, educational and religious activities. Groups desiring professional status should urge their members to bring their judgment and experience to the councils of government, legislative halls, and organized efforts for the benefit of their communities. In doing so they reveal those qualities of mind and character that earn prestige and confidence, and they reveal them to a far wider circle than their immediate clients who presumably know their virtues already.

A degree of selflessness is looked for in the professions. Made up as they are by human beings, this quality is not uniform. Some individuals achieve it more than others, and some professions more than others. None of them is expected to go broke in the process. To do so would defeat the end of service. But the public expects a certain altruism of the professions; people have come to recognize it as a hallmark of professionalism, and they accord professional status more readily to those vocations that exhibit it than to those that do not.

A Code of Ethics

It is characteristic of the professions that they govern themselves by a code of ethics devised in the public interest as well as to protect the members themselves. These codes proclaim that the members of a profession are dedicated to applying their talents to the public's benefit. They also lead members to behavior which will attract the public's confidence. People have to trust a professional man because they have few ways of appraising his work. They frequently must take his competence on faith. John L. Carey, Executive Director of the American Institute of Certified Public Accountants, has pointed out that ethical codes of true professions can do much to insure competence and the proper use of that competence. He also notes that "good ethics are good business."

Codes Known to Exist

While these codes are generally known to exist, the public seldom sees evidence of them, and people tend to forget how well they are protected against abuses of their confidence. When they do glimpse ethical codes at work, they are reminded at once that they are witnessing true professionalism in action. The lawyer disbarred, the minister unfrocked, the CPA deprived of his certificate, all these represent the powerful censure of the offender's peers and a warning signal to the public. These measures are taken with painful deliberation and usually with distaste. It is an unpleasant duty to deprive a professional man of his good name and, frequently, his means of livelihood. Perhaps compassion is one reason why such discipline is often dispensed without public notice. Or perhaps the judges are loath to disclose the existence of malpractice.

Whatever the reason, one of the important and symbolic attributes of professionalism is less visible to the public than it might be. Vocations aspiring to professional recognition and those desiring to reaffirm their status might well consider whether disclosure of ethical machinery at work is not only an obligation to the public but a logical method of achieving their goal.

Independence

The independence of the professional man distinguishes him from the crowd. Wise kings had little use for a vizier who was a yes-man. If a lawyer, CPA or public relations counsellor lets other considerations interfere with his professional judgment, what use is his advice to the client? Success in a professional career has a lot to do with persuasiveness. The fear of losing a client, which is the chief reason for lack of independence, is a poor foundation for persuading him.

There is some danger of a misconception spreading among many professional people that it is "good public relations" for them to look more and more like the other fellow on Main Street. This belief is nourished in part by the 20th century trend toward conformity, a trend, incidentally, which makes the public relations task of sharpening images that much harder.

This is not a plea for eccentricity. There are good public relations reasons why a professional man should establish membership in certain clubs, drive a suitable car and otherwise maintain an acceptable

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Opportunities for Broader Management Services by CPAs

By William L. Campfield

During the past five years, the public accounting profession has exhibited increasing interest in extending its services to management beyond the limited confines of opinions on financial statements, accounting system review and installation, tax work, and similar services related almost exclusively to historical financial data. For example, the American Institute of Certified Public Accountants through its Committee on Management Services by CPAs has prepared several articles and bulletins classifying and delineating the variety of management services which are within the present or easily attained competence of certified public accountants.

Notwithstanding this worthy interest and work on the part of the premier organization of professional accountants, the writer believes that additional attention and effort need to be devoted to focusing the expanded services of public accountants more closely on matters that lie at the very heart of the management process. It is the purpose of this paper to set forth, in skeletonized form, some of the significant general management areas in which the unique knowledge and experience of public accountants can be used in practical assistance to individual managements in better planning, coordinating, and directing the over-all activities of their respective enterprises. The areas covered are: (i) planning for long term growth and service, (ii) market research and analysis of consumer demand, and (iii) improving the internal communication system of the enterprise.

A portion of the work to be performed by the public accountant in the foregoing areas could be accomplished as adjuncts to his conventional examination of financial statements. However, the bulk of the expanded service is likely to require special analysis and examination apart from the conventional audit.

One further preliminary observation is in order. It is obvious that the public accountant must prepare himself and staff, if any, in the special additional knowledge, skills, and attitudes necessary to render the expanded management services. For the accountant to assume such responsibilities without appropriate preparation would be short sighted indeed.

It is not deemed essential to the development of the balance of this paper to discourse on the methods or techniques by which the public accountant and staff should acquire the necessary knowledge and skills nor on the details of application of

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such knowledge and skills. Public accountants have in the past exercised resourcefulness and ingenuity in preparing themselves for broadened responsibilities. They can be expected to continue this tradition in the future.

Facilitating Long Range Planning

It is commonplace in mid-20th century that the long range continuity and profitableness of a large scale enterprise depend on the skill and timeliness with which its management achieves a delicate balancing and synchronization of the economic and human values affecting the enterprise. The rights, duties, and rewards of the many people who comprise an enterprise, do business with it, or have responsible interest in it must be considered by management within the policy, structural, and operational framework of the enterprise. Ineptness by a management in this regard could have disastrous long term effects both for the enterprise and for society as a whole.

Since the well trained and skilled public accountant has experienced a wide and diversified range of economic transactions and business viewpoints, he is well equipped to aid a management in the formulation of policies and decisions. Accounting methodology and auditing techniques which he normally uses to accumulate and communicate economic facts about an enterprise can be expanded into an instrumentality for promulgating policy, plans, and programs.

Three specific sub-areas of planning in which public accountants can expand their services to management are discussed in following paragraphs. They are: (i) assisting in the construction of the framework or mold of the long range plans which establish the institutional characteristics of the enterprise and its more or less permanent image, (ii) establishment of the methods and environment in which flexible, constructive planning is continuously initiated, reviewed, and adjusted to accommodate changes in enterprise operations and growth, and (iii) accumulating and analyzing relevant basic data, and screening alternative plans for the purpose of assuring that top management's decision making is directed expeditiously to well conceived and important alternative courses of action.

The long term objectives and broad policies of an enterprise furnish the framework from which all management decisions are drawn. Clearly formulated statements of the "basics" serve as a unifying guide in determining specific project and period plans and programs, selecting resources, and in conducting and evaluating operations. Included in such statements should be concise and positive identification of such important factors as: (i) the industry and societal leadership level sought by the enterprise (this determination will materially influence the diversification and quality of product or service, size and scale of plant, pricing policies, labor relations, community activities, etc.), (ii) the degree to which the enterprise will emphasize dynamics or stability in operations, and (iii) the broad aspects of administration to be practiced, i.e., whether centralized or decentralized administration, type of key administrators and other key personnel to be employed, kinds and range of advance planning, and the like.

The well versed public accountant can be especially useful in synthesizing accounting, economic, and other

statistical data which top management can use in constructing the basic policy and mission framework. In the case of a fairly new enterprise or an established one which proposes to materially alter its corporate image, the accountant's initial contribution could be the systematic development of the data regarding prospective demand for products or services of the industry as a whole, factors affecting key supply sources, trends and changes in competitive conditions within the industry, and pro forma estimates of the relative standing of the enterprise with respect to share of markets, cost position, and competitive strength.

With respect to the process of formulating long range objectives and goals, it is important to note that at some point of time the management of a growth enterprise must determine the definite role the enterprise will play in the economy, the specific mission which the enterprise will undertake on a long term basis, and the paths which rationally lead to continuously profitable and socially useful accomplishment of that mission. These determinations usually represent the initial definitive stage of development of the institutional character or image of an enterprise. Since the modern concept of planning is tied to the notion of influencing events to happen that would not otherwise occur, it is quite apparent that the accountant who furnishes substantial assistance to management in constructing the matrix for long range planning will have made an important contribution toward giving the enterprise greater influence over its destiny.

The second major area of policy making and planning in which the public accountant can extend his services is that of aiding in the establishment of adequate methods and an enterprise environment which insure continuous long term and short range planning, review and analysis of such planning, and timely synthesis and adjustment of plans to take advantage of social and technological changes and innovations.

Effective control of the over-all planning process will require that top management (and the public accountant to the extent that a significant portion of his time is devoted to counsel and assistance in the planning process) free itself from routine decision making in order to concentrate on the larger and more important task of plotting the long range future. To achieve this freedom essential for conceiving the premises that underlie all planning and consummation of plans, top management must have prior assurances that the enterprise has a soundly devised and operating organizational structure and relations, an effective system of control, appraisal, and measurement of actual operations, and above all has fully qualified and imaginative personnel in all key positions. It is taken that the public accountant will draw upon his store of knowledge and experience to help management obtain these prior assurances.

One of the most important reasons for planning is the opportunity to profit from anticipations of technological, political, and social changes which affect an enterprise. In order to take advantage of innovations and thus guide them along constructive lines, the management of an enterprise must 'plan its planning' in a way to achieve flexibility of the type of military plans. The latter normally consist of a long term and broad strategical plan together with the alternative courses of action or tactics that must be undertaken to meet requirements of temporary interim developments without abandoning the

basic long range program. In analagous fashion, an enterprise must arrange its over-all planning in a manner to permit quick tactical maneuvers, where required, within the broader policy or strategy framework.

The public accountant might well assist top management in establishing an orderly system for allocating responsibility for design of plans, progress review of plans in action, and post-action evaluation of the effectiveness of the plans. The over-all planning scheme would call for appropriate distinction, both as to content and responsibility, between the substantive planning involving broad enterprise policies, missions, and goals and the procedural planning associated with programming and scheduling of specific projects and work detail.

Inasmuch as the public accountant's conventional audit examinations bring him into close contact with personnel and activities "across the board," he should not experience much difficulty in helping management create an action-centered planning climate from the top down. Important elements to be considered in creating this climate are assignment to each key individual of some definite time-phased part of planning, the grant of clear cut authority commensurate with responsibility for planning, and the establishment of strict accountability for accomplishment of assigned phases of planning.

A third area of policy making and planning in which the public accountant can be of assistance is that of developing or improving the actual decision making process. Much has been written in recent years about the nature of decision making and the modern scientific methods and techniques available to management for making decisions. However, the writer believes that the element of mature judgment essential to substantive decision has not been sufficiently stressed in the literature. Moreover, the frequent emphasis on the mathematical or statistical aspects of decision making has influenced an inordinate amount of attention to "decisions by formula." In these circumstances, the seasoned public accountant could well serve as the catalyst in the management effort to improve the quality and adequacy of decisions.

It is to be expected that, as a result of a carefully conceived planning climate and related assigned responsibility, there will be prepared for top management's consideration a series of detailed alternative project and period plans. The accountant can be especially helpful in assuring management that the planning system is operating in a way to produce acceptable action plans. He can also be useful in performing advance screening or analysis of plans submitted by subordinate personnel in order to minimize the number of alternative plans which a top management need review in detail before arriving at long range decisions.

It is well known dogma in modern management that there are numerous plans or programs applicable to a given situation, any one of which may work reasonably well and result in some predictable degree of profit. It is far more important to the welfare of the enterprise that a judicious and timely selection be made of one of the plans and job performance started than to prolong analysis and deliberation until the last shred of doubt has been removed as to which plan is the most profitable. In this connection, the public accountant could assist in speeding up the decision making process by reviewing or supervising the review of each of the major alternative plans prior to submission for

final decision by top management. His review and analysis could be pointed to identifying for the attention of management those plans or strategies which most nearly conform to management's criteria for preferred plans. Final selection of the plan or strategy to be adopted could then be made by top management with the assurance that all worthwhile alternatives had received adequate advance review and consideration.

In concluding this portion of the paper, it is useful to remind ourselves that top management has the difficult yet compulsive responsibility for anticipating the shape and content of future events which will affect the enterprise. Moreover, management must exert every informed effort to influence the environment in which the enterprise operates, not merely adapt the enterprise to the existing environment. The public accountant's greatest opportunity for increased service to top management is, therefore, likely to be fulfilled when he helps to assure that management that the key information needed for major decisions is accumulated and presented in a way that the management hierarchy can understandingly grasp required facts early and make decisions quickly and confidently.

Counsel in Forecasting Long Term Demand

Determination of the shape and content of consumers' satisfactions is an elusive and enormous task. Involved in the concept of consumer demand are a myriad of rapidly changing individual and group ideas about the kind and value scale of human desires, the costs and difficulties to be overcome in their satisfaction, alternative or substitute values in products and services, and the constant flux in knowledge and facilities available to satisfy human wants.

All of the foregoing point up rather strikingly the necessity for an enterprise management to make very careful advance analysis of present and future demand for its products and services. A reasonably steady and predictable demand is the life line of business enterprise. The actual production output and scale of plant can only be plotted after a determination has been made of anticipated sales volume. It follows that the entire constellation of internal management problems of programming, correlating, and controlling enterprise operations is inextricably interwoven into the broad enterprise policies regarding consumers and consumer demands.

In the circumstances, an alert management will develop or secure all the methods, techniques, and services essential to the collection and publication of up to date information relating to current and potential demand for its products and services. The well rounded and experienced public accountant by the very nature of his association with many enterprises and many markets is one of the most valuable sources of assistance to which the reasoning manager can turn.

In the economic system under which modern enterprise operates, the knowledge of relevant economic facts is diffused throughout society. Conventional economic analysis focuses upon *the pricing system* as the coordinating force which merges the separate economic actions of many people into an integrated whole. It is reasoned that the price system reflects the ultimate decisions of the multitude of persons who are familiar with the resources of a society and consumers' desires for the use of resources.

Helpful as the above theory may be for purposes of aggregative economic analysis, it is quite obvious that the important consideration for the individual business is not price theory in general but a workable price theory for the individual firm. A galaxy of interrelated postulates will be necessary to derive such theory. In part, consideration must be given to such factors as: (i) type, size, location, disposable income, buying habits, etc. of potential consumers, (ii) the line and quality level of products and services to be offered, (iii) price and quality of competing products and services, (iv) the general price level, (v) anticipated demand for the firm's products at various tentative prices, and (vi) estimated cost of production and distribution.

In most businesses it is customary to establish prices for some relatively long term. Generally, because of existing contracts or because of habitual buying habits of consumers, it is not feasible to change these prices too readily. Hence, the price structure and price theory of a firm once established become fairly widely known and permeate the entire fabric of enterprise-consumer-society relations. In a sense, it may be said that the firm's price theory and the related price structure condition the entire activities of the enterprise. From it flow consumer and sales policies which broadly define the shape and volume of economic service to be performed, policies as to output and scale of plant, and all other policies governing internal operations.

From the foregoing, the conclusion is apparent that when a business management undertakes the construction of a workable price theory for its firm it is faced with a multi-variate and multi-dimensional problem. It follows therefore that management must establish adequate internal machinery which will keep it continuously and reliably informed as to reasonably anticipated demand and of tested ways and means for promoting increased demand. In addition to establishing a smooth internal data gathering and analysis mechanism, a management should secure sufficient outside specialists to make systematic review and evaluation of the firm's price and consumer policies "in action." As mentioned earlier, the firm's public accountant can render valuable assistance to management in synthesizing the results of study and analysis by the outside specialists.

Successful prediction of the general direction in which an enterprise is headed necessarily involves a degree of detachment and objectivity not always possessed by the managers who are closest to the surface data. Public accountants, through renewed efforts to improve the factual bases upon which economic data are presented, can contribute inestimable aid to a management in its quest for a sound platform from which to launch its forecasts of long term demand for its products and services.

Prior to concluding it might be helpful to point out some frequently neglected areas to which specialists, both internal and external, should give added attention in aiding management to keep on top of its responsibility for insuring long run demand. Greater emphasis needs to be devoted to ways and means by which individual enterprises or a concert of enterprises can legally change or stimulate consumers' desires in a socially beneficial manner. A particularly fruitful area for added attention is that of study and analysis of consumer motivation, i.e., determination of the motives behind consumer purchasing. As

a corollary, controlled experiments might be conducted to ascertain the actual changes in consumer desires or purchases that can be induced through varying types of promotion.

In summarizing this part of the discussion, it is relevant to note that the public accountant, experienced as he is in analysis of sales and revenue data, can render service of major import by helping a management achieve a relatively ideal continuous analysis of potential demand. This ideal should yield results permitting formalization of prices over reasonably long periods and at the same time contain sufficient flexibility to permit management to make timely adjustments to compensate for major changes in consumer demand.

Aid in Improving the Enterprise Communication System

In today's monolithic enterprises there is typically a wide gap between the top administrators and the workers down the line. Since the latter group is the one which must actually perform the work envisaged in management's policies, plans, and programs, a management must assure itself that the meaning as well as the form of its messages is being adequately communicated.

Management generally encounters little difficulty in devising a reasonably effective system and media for physically transmitting information throughout the enterprise. It encounters problems in two basic areas: (i) assuring that in the downward flow all important plans and policy messages get to the people who need them in sufficient time to be used as a basis for action, and, as a corollary, that there is a reasonable meeting of minds all the way down as to the meaning of the messages, and (ii) assuring that in the upward flow important information required by top management for policy making and control is neither delayed nor improperly siphoned off at various subordinate levels.

It is not unusual for a public accountant, who serves an enterprise on a continuing basis, to review and test the adequacy of communication media, methods, and arrangements. For example, independent accountants, as part of a continuing service, frequently make inquiry and test the methods by which supervisors transmit orders and instructions to workers, the methods and media used by various levels of administration and supervision to disseminate policy and other information, the methods, media, and techniques used in job training, and so on.

In addition to the foregoing ways in which the accountant can offer constructive information and recommendations to management, the writer proposes that the public accountant work actively with top management in developing a clear cut philosophy of communication for the enterprise. A first consideration is a clear understanding at the top management level of the kinds of information that must be communicated expeditiously and meaningfully to workers if optimum joint action and participation is to be achieved. A second consideration is the assurance that each key member of the management hierarchy has or will acquire early an understanding and sensitiveness to the ways in which ideas and motivations are communicated from one mind to another. Obviously, little difficulty is to be expected in communicating fairly standardized and routine ideas, instructions, and the like.

In the course of his conventional financial audit, the public accountant

is likely to obtain valuable clues regarding the specific policy and media and other information which are not being properly understood or interpreted down the line. However, the accountant must acquire additional skills and insights before he can contribute the full measure of his potential assistance to management in the area of communications. As a minimum, he must acquire added familiarity with the fundamentals and basic techniques of motivational theory. This will permit him to synthesize and integrate the findings of personnel administrators and humanation specialists with other relevant data that he develops on his own initiative.

The emphasis in the foregoing discussion has been limited to ways of improving the internal communication system of the enterprise. To be sure, the philosophy and methodology underlying external communication, i.e., with customers, creditors, general public, etc., must be soundly conceived and practiced if the enterprise is to enjoy long lived profitableness. However, this subject deserves a fuller discussion than would be relevant in this paper.

In concluding this section, we may generalize that communication is a valuable attitude and skill to be used by management in creating productive and profitable understanding throughout an enterprise. It has been fairly well established that human beings have a high degree of native creativeness and that they wish to cooperate with others in translating this creativity into things useful to society. Consequently, it is an important task of management to communicate its objectives, goals, plans, and programs in language that not only is clear and concise but which expresses a definite spirit that identifies the well being of the enterprise with the intelligence, capacity, and well being of each individual in the enterprise who must carry out the directions of enterprise management.

A considerable portion of the public accountant's background and experience has been focused upon communicating economic ideas to others through the medium of accounting, auditing, and statistical reports. With a minimum of additional study and experience with the theory and techniques used in the broad fields of communication and motivation, he should be eminently qualified to help a management make substantial improvements in the communication philosophy and practices of its enterprise.

Summary

The modern concept of efficient management is tied to the notion of influencing profitable events to happen that would not occur except for careful foresight and planning.

As decentralization of modern enterprise increases and related skills and abilities are widely diffused, it becomes abundantly clear that an enterprise management must rely more and more on experienced, independent and objective individuals and media to keep it informed intelligently and timely on the course and trend of enterprise activities.

Public accountants have for many years served enterprise managements usefully in furnishing objective opinions on financial statements, installing and reviewing accounting systems, and performing other work concerned primarily with historical financial data. Necessary as these services are for the management of business enterprises, they do not represent the full potential of service

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Some Causes of Ineffective Administration

By Ray E. Brown

Effective administration has proven to be a most necessary element of the highly developed and complex environment which we moderns have created for ourselves. A jet-stream of scientific and technological advances in every direction has opened the way for a more productive, more leisurely, and healthier life. These same advances however, have so enormously complicated our efforts toward this more abundant life that we have had to highly organize our means and our efforts for work, for play, for health, and even for worship. This need for planning and direction has created a multiplying need for competent administrators to manage all those activities in which we work, or which work to serve us.

The swelling demand for competent administrators has created a man-hunt of immense scope on the part of the almost countless number of firms, agencies, and institutions that make up our economy and our society. Naturally, a man-hunt calls for a description of the party being sought. In recent years considerable effort has been devoted to the problem of describing the characteristics of the effective administrator. Successful administrators have been cross-sectioned at work, at home, and at play in an effort to ascertain the common traits possessed by those who have demonstrated competence. As one reviews these efforts he is impressed with the similarity of the list of characteristics of the effective administrator and those usually ascribed to the average good citizen. Certainly the effective administrator must be honest and loyal, possess integrity and enthusiasm, and love his fellowmen if he is going to be allowed to run loose in society and not be avoided by his own secretary. It is very doubtful, however, that he can parlay those virtues alone into a successful career as an administrator. Possession of the proper traits and skills is not in itself sufficient. It is their appropriate use by the administrator that determines the degree of administrative success. From the same piece of steel one may fashion a lock or a burglar's tool for breaking the lock. Administration simply cannot be judged by the segmental attributes of the administrator but rather by his total actions and reactions. Administration is practice in situations and is also the practice of creating situations. It is what the administrator does, or does not do, that

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produces an effect on the organization. Said in other words—it is administrative behavior that determines the sorts of influences the administrator will have on the organization.

An attempt to define proper administrative behavior requires the inclusion of so many elements of ordinary good behavior that one ends up in pretty much the situation as have those who have attempted to describe the traits the good administrator must possess. For this reason it is my feeling that new and added information on the problem of profiling the effective administrator might be secured if we reversed the usual approach and examined some of the behavioral characteristics of the ineffective administrator. The following generalizations represent such an attempt. These generalizations are compiled in part from discussions with persons who have experienced marked failure in administration and also with persons who have had marked success in administration. Those discussions were necessarily of a leading and directive character, inasmuch as one cannot expect individuals to demonstrate much more insight in reviewing their experiences than was demonstrated when they were undergoing them. Also, as one might suspect, a considerable portion of the observations represent reflections on my own conduct as an administrator. Actually the characteristics observed are very human characteristics and perhaps never completely eliminated. Successful administration seems dependent, however, on successfully modifying their inhibiting effect on administrative behavior.

One of the most common characteristics of ineffective administration is the tendency to attempt only perfect solutions instead of the accomplishable. This can be described as the all or none complex. Administratively this all or none complex leads to two extremes—both of which are harmful to the organization. On the one extreme it may mean that improvements are never undertaken because the ideal solution isn't currently available or possible. Necessary changes are never accomplished because the opportunity for perfect solution rarely comes along. Major changes are always difficult to accomplish, and even the bravest and most energetic of administrators are sometimes tempted to rationalize their distaste for facing up to those difficulties by waiting for the perfect solution.

On the other extreme it may mean that the action undertaken is too radical and the organization is subjected to turmoil and violent upheaval. Under these circumstances the changes attempted may be ultimately correct but currently just not accomplishable. Such moves ignore the necessity for administrative timing. The successful administrator must, on occasions, tolerate conditions of inefficiency rather than court failure by attempting to clear all the obstacles with one great push. He must determine his goals and evaluate the opposition to them. This permits him to maintain constant pressure toward the desired ends without allowing the pressure to explode into an open break. It also makes him willing to accept and attempt alternatives if they move toward the ultimate objective. Among his repertory of virtues the effective administrator needs a high frustration level. Somewhere between the extremes of procrastination and those of abortive change the effective administrator finds the path of consistent progress. By proceeding along

that path, step by step, the administrator can ultimately achieve his long range plans and at the same time secure the personal stimulation, so necessary to his own morale, that derives from immediate accomplishments. It will help the administrator if he keeps constantly in mind the fact that apparently ideal solutions are themselves only estimates at a given time and are subject to the many errors inherent in predicting results of human activity. In this sense all solutions are only proximate ideals and never absolute ideals.

Before someone interprets the above as an argument that the good administrator is afraid of his own shadow, I must point out an opposite characteristic that is equally as conducive to ineffective administration. This is the urge to act from expediency—the attempt to buy our way out of problems by yielding to immediate pressures and ignoring the long run effects of the solution. Sidestepping an important issue is just as bad as stiff-arming it. In some ways it may be worse because it permanently weakens the administrator's influence in the organization. Yielding to the pressures of the moment is an open invitation for a raid by the most aggressive and most vocal members of the organization. It is a sort of cafeteria administration in which everyone strong enough picks out his own policies. It is properly interpreted by other members of the organization as evidence of indecision and uncertainty and, organizationally speaking, the only thing worse than a bad decision is indecision. It demonstrates a lack of convictions as to long run goals or else an unwillingness to stand up and be counted on issues important to the welfare of the organization. Either situation results in administration by default. A policy of peace at any price has seldom produced peace but has always raised the price. In this connection it should be pointed out that administration is not a popularity contest and that many administrative decisions represent choices between opposing views within the organization. This is particularly true in hospital administration because of the diversity of interests represented, when measured in the short run. While all groups externally and internally involved may have the same long term purposes, their daily interests are not so clear and unified. Under such circumstances it isn't possible to have all sides like all decisions, but it is possible and important that they respect them.

The failure or inability to weigh the implications to the organization of decisions based on expediency may produce two unfavorable results. As in all cases where the treatment is aimed at the symptoms rather than the cause, it may mask the basic cause of the problem and thus prevent the solution when the solution is easiest accomplished. Administration is not a game of solitaire that can ignore the rights that individuals develop in precedent and established practices within an organization. The results of expedient decision may not come to a head until long after strong organizational habits have been developed and strong claims staked out on the basis of those decisions. Corrective measures usually take an even longer time to implement unless upheaval is to result. The trauma to the organization is bound to be greater when circumstances are not corrected and encouraged to grow into situations. Another unfavorable result from decision-making on a first-come-first served basis is the damage to continuity of policy. Perhaps no requisite is as important to an organi-

zation as that of predictability of administrative reaction. It is the only way the administration can influence the hundreds of decisions made at all work levels in even the smallest of organizations. It is tough enough to develop an organization that wants to do what the administration wants done, but it is impossible to accomplish the administration's wishes unless those wishes can be predicted. Without consistency in decision-making at the top level there is no basis for predicting administrative wishes at other levels in the organization. Zig-zag decision-making imposes an intolerable burden on those who have the task of keeping in step with the leader.

The obsession to win represents another serious handicap to administrators. This is often demonstrated in the attempt to win a "moral victory" even after decisions have been clearly discredited. Too much emphasis is given in administration to the necessity of saving face and not enough thought paid to the problem of saving respect. The administrator may silence but he cannot fool those responsible for carrying out an impractical decision. If face saving is really important it would seem better strategy for the administrator to sweep his errors under the carpet as quickly as possible rather than to give them the prominence that results from the disgruntlement and ill-will of those compelled to operate with them. As every kid knows, the best thing to do with a lemon is to make lemonade out of it. It is surprising how many improvements in administration have come out of things that went wrong. It is very possible that we learn more from our failures than our successes. The administrator should consciously develop the ability to lose a point gracefully. In too many instances we not only finally lose the point but we succeed in losing the goodwill of those involved. The effort to perpetuate an error can sometimes eat heavily on the time and energy of the administrator. But more important is the way it chews on his disposition. This is demonstrated by the feeling of relief and even pride one experiences on those occasions when he is big enough to admit he was wrong.

The obsession to win at all costs is the largest single deterrent to full participation by colleagues and subordinates. There can be no battle of ideas within the organization if the reward is disfavor and ill-will from the boss. The willingness and the ability to permit decisions to be discussed and pulled apart before committing the organization to follow them represents about the only method available for pre-testing of administrative ideas. The administrator deals in ideas and these, unlike objects and goods, cannot be tested in the model stage before placing them on the market. Permitting colleagues to participate in decision making is not so much a favor to the participants as it is a favor to the administrator. It not only permits pre-testing of decisions and ideas by exposing them to the scrutiny of those who will have to use them, but it assures support instead of sabotage. Human nature being what it is, there is no better way to insure support, as well as defense, than to involve others. To coin a phrase, this represents conspired leadership and such leadership is probably the most adhesive of all.

High among the factors which contribute to ineffective administration is the tendency to classify everything as black or white—as all good or bad. This fault denies the fact that it is the administrator's task to discriminate between acceptable alternatives

more often than between right and wrong. Situations are rarely ever black or white but are usually varying shades of gray. At least, if the administrator is fulfilling his proper function, only the gray decisions will reach his desk. The easy ones will be settled down the ladder where the facts are more abundant. Problems which are screened to the top level of the organization usually carry with them the troubled ponderings of those involved along the line of ascent. Whether the need is for choice between conflicting views, or reassurance as to proper direction, questions reaching the top level must be treated with respect. Such respect may dictate an audience with the individual or individuals involved. This not only demonstrates interest and concern on the part of the administrator but reveals both the facts and the feelings that produced the problem. The feelings often give more weight to a problem than do the facts. When a person is disturbed, the facts can turn quickly into fancy and the two must be carefully unraveled before a solution will be fully accepted.

The urge to use the black-or-white technique in administration is a strong one and can develop from several directions. The deficit of time which always plagues the administrator doubtless causes him to seek quick answers. The housekeeper instinct to get things settled and the file off the desk can lead to quick off-the-cuff decision. In other instances emotional factors can cause the administrator to pick sides and thus eliminate the bother of looking at the other side. The proven advantage of decisiveness in administration may also be a strong factor. The urge to simplify problems can, of course, represent an important asset of the administrator if it is tempered with the knowledge that the etiology of most management problems is multifactorial and multi-sided.

Somewhat related to the all-or-none complex is the failure to maintain a sense of proportion—a sense of balance in administration. This fault manifests itself in several ways in administrative behavior. One of these is best described by the old expression "making a mountain out of a mole-hill." It results in over-emphasizing incidents and problems that have little consequence to the organization. It not only wastes the energies and attention of the administrator but it diminishes the influence of the administrator on matters that are important. Subordinates easily develop organizational calluses for this reason and both the whip and the sugar should be given only when circumstances warrant. The fault is also exhibited by administrators who are unhappy unless they skin an elephant every day. They find it difficult to properly distribute their enthusiasm and energies and have interest only for the big projects and the big deals. Even the interest in the big deal isn't sustained and it also soon suffers from inattention.

The demands on the time and the energies of the hospital administrator make it mandatory that he learn to put first things first. Administration is always a matter of selective attention—of recognizing the significant. This is so important that every administrator should preview his activities each day and allocate his time and interests to those problems and matters with highest priority. If he does not do this he cannot avoid practicing administration by random instead of by plan. This means the administrator's attention is devoted to the problems of the more verbose and forward members of the organization rather than to the more important and timely

problems. It also means that the administrator is unable to properly delegate responsibility because he never knows what to delegate. It demonstrates he is able to carry a load but not smart enough to share it. The insecurity that is bound to result from failure to exercise selective attention may be the reason that some of us never quit worrying — even about problems that are already solved or that never existed.

The failure to maintain an impersonal status in the organization can prove to be a serious handicap to the administrator. He must protect a sufficient area of aloofness to permit administrative action without it being taken personally. Admittedly, he must be responsive and friendly so that his colleagues will not hesitate to approach him. But he must recognize the difference between liking his associates and liking everything they do. Personal relationships that inhibit detached evaluation and frank criticism represent a disservice to all concerned. Criticism is fundamental to improvement and every member of the organization has a right to expect that he will be told when his performance needs improvement. Nothing shakes the morale of an organization as much as the suddenly letting down of the boom on an individual without prior effort to improve his deficiences. The rules of fair play are applied more strictly to the administrator than to anyone else and these rules require that a person be told where he stands and why.

The necessity for fair criticism might seem at variance with the "sweetness and light" doctrine one hears preached so often today. If that doctrine means the administrator has no right to show and express irritation, it is indeed at variance with proper administrative conduct. Just as the administrator should demonstrate approval for a job well-done, so should he demonstrate disapproval for faulty performance. It's the only way the organization can determine the level of performance expected by the administration. The important thing is that the administrator be able to demonstrate irritation without demonstrating hostility and without creating antagonisms. Only by reserving a margin of impersonal relationship can he hope to appear emotionally casual as he carries out his daily task of modifying human conduct.

This matter of human conduct brings us to another cause of ineffective administration. This is the mistaken assumption that people act logically. Individuals usually do not act either logically or illogically when they are personally involved. In such instances they are most apt to act non-logically. This is because they are persons and bring to every situation their own personal experiences, biases, desires and needs. Situations are seen from each individual's own uniquely personal perspective. This requires that the administrator at times must temper his decisions to allow for the personal equation and to work toward the modification of preconceived notions of those affected by his decisions. The fact that individuals have changing value patterns and motivations, and that these change more rapidly than we think, makes such modification possible. It also requires that the administrator learn those with whom he works without stereotyping them. It means that he must realize that his own outlook also is subject to change as he has new experiences. His own reactions have the same tendency to be compatible with his own personal desires. To

whatever extent possible he needs to be cognizant of his personal biases and to allow for these in his evaluations of people and situations. At the same time it is highly important that he maintain respect and confidence in his own judgment. He simply cannot command any more respect from others than he has in himself.

The attempt in this paper has not been to outline all the factors responsible for ineffective administrative behavior. Further study would doubtless bring out equally important causes. Rather it has been an attempt to emphasize the importance of behavior as contrasted with segmented skills and traits. Administration requires many various skills and knowledges but they are effective only to the extent they are integrated into a balanced practice of administration.

The Image of Professionalism

(Continued from page 15)

standard of living. But should his office be indistinguishable from the offices of business executives? Must he emulate the crowd in his personal appearance? Must his taste for reading, music, pictures on the wall of home or office conform? Public relations should counsel independence. It should not let the professional man lose his identity in the happy-go-lucky throng of back-slapping boosters who parade their enthusiasms in the very name of "public relations." On the contrary, his character must not become blurred until he is lost in a sea of homogeneous American businessmen. He can sharpen his image as a professional man best by being himself and throwing his full force into his role as a learned, wise, ethical advisor, concerned with the common good.

TAX COMMENTS

Conducted by the Committee on Taxation of the Illinois Society of Certified Public Accountants

THE STATE INCOME TAX DILEMMA

On February 24, 1959 the United States Supreme Court, in the *Northwestern States Portland Cement Company* and *Stockham Valves and Fittings, Inc.* cases, opened a veritable Pandora's box on an unsuspecting business public. In essence, these decisions stand for the proposition that a state may levy an income tax on an out-of-state business which is engaged *solely* in interstate commerce in the taxing state.

In the *Northwestern States* case, which involved the Minnesota income tax, the company was an Iowa corporation, not licensed to do business in Minnesota. It leased a sales office in Minneapolis, occupied by three employees—two salesmen and a secretary. The company employed two other salesmen in Minnesota who used the office as a "clearing house." The company maintained no bank account in Minnesota, owned no real estate there, and warehoused no merchandise there. All orders received by salesmen in Minnesota were subject to acceptance at the company's home office in Iowa, and all merchandise was shipped to customers from Iowa. A finding of the lower court, not challenged in the presentation to the Supreme Court, held specifically that all of the company's activities in Minnesota were wholly in interstate commerce; the company conducted no intrastate business there.

In the *Stockham Valves* case, which involved the Georgia income tax, the company was a Delaware corporation with its principal office and plant in Birmingham, Alabama. It leased a sales-service office in Atlanta, occupied by a full-time secretary and by one salesman who devoted about one-third of his time to soliciting orders in Georgia. All orders received were subject to approval at the Birmingham office, and all merchandise was shipped to customers from Birmingham "f.o.b. warehouse." The company owned no property in Georgia, other than office equipment and supplies, warehoused no merchandise there, and had no bank accounts there. Here, as in the *Northwestern States* case, the company was engaged solely in interstate commerce in Georgia.

Because of the similarity in the cases, the Supreme Court considered them together and issued an opinion covering them both. The Court summarized its decision in the following sentence: "We conclude that net income from the interstate operation of a foreign corporation may be subjected to state taxation provided the levy is not discriminatory and is properly apportioned to local activities within the taxing State forming sufficient nexus to support the same."

There are three elements in the Court's statement—(1) the levy

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must not be discriminatory, (2) the income must be fairly apportioned to local activities within the taxing State and (3) the local activities must form a sufficient nexus.

On the first element, there is no present state income tax statute which levies a tax which discriminates by its terms between foreign and domestic taxpayers. On the second element, the taxpayers in the *Northwestern States Portland Cement* and *Stockham Valves* cases raised no question as to the fairness of the apportionment formulas involved. The Supreme Court commented that the possibility of multiple taxation exists in this type of case, because of the difference in the apportionment formulae used by the various states, but that it is up to the taxpayer to show that a given formula places a burden on interstate commerce in a constitutional sense. Since that issue had not been raised, the Court was not obliged to consider it.

What Is A "Sufficient Nexus?" The third requirement laid down by the Court is a sufficient nexus between the taxpayer and the taxing state based on local activities. Since immunity from state taxation based upon interstate commerce has now been struck down by the Supreme Court, and since it may not be possible to prove that the levy is discriminatory or that the apportionment formula is unfair, about the only defense which remains is a claim that the taxpayer does not have a sufficient connection with the taxing state to support an asserted tax. It is now clear that a sales office in the taxing state is a sufficient connection. It is very likely that the presence of traveling salesmen in the taxing state, without a sales office, is sufficient. In *International Shoe Co. v. Washington* [326 U.S. 310 (1945)] the Supreme Court held that the frequency and extent of that company's business contacts within the state (based on the continuous activities within the state of a number of traveling salesmen) were sufficient to give the state jurisdiction over the company to collect unemployment insurance contributions. Several states have already announced that they intend to tax out-of-state businesses whose only contact with the state is one or more traveling salesmen.

The tax administrators of at least one state go a good deal further than this. At the recent annual meeting of the National Association of Tax Administrators, held in Buffalo, New York on July 8, 9 and 10, the representatives of the State of Georgia declared that they believed that they could properly assert a tax against any out-of-state business which made any "economic penetration" of that state by delivering merchandise to a customer in the state, no matter how the order was secured. Thus, advertising into the state by radio, television, newspaper or periodical, or by direct mail, followed by mail-order sales to Georgia residents, would be a sufficient connection in the opinion of these officials.

How Broad Is The Problem? The extent of the problem is indicated by the fact that at the present time thirty states levy a tax directly on net income, and so are in a position to assert a tax on interstate commerce under the *Northwestern-Stockham* doctrine.

These states are: Alabama, Alaska, Arizona, Arkansas, California, Colorado, Delaware, Georgia, Hawaii, Idaho, Iowa, Kansas, Kentucky, Louisiana, Maryland, Minnesota, Mississippi, Missouri, New Mexico, North Carolina, North Dakota, Oklahoma, Oregon, Pennsylvania, Rhode Island,

South Carolina, Tennessee, Utah, Virginia and Wisconsin.

With the increasing revenue needs of the states, it is reasonable to expect that other states will enact similar legislation. In the aftermath of the *Northwestern-Stockham* decision, three states—Tennessee, Idaho and Utah—have already joined the ranks.

There are two elements to the problem faced by businesses operating in interstate commerce—the tax cost and the compliance cost. For many small and medium-sized businesses, the tax cost in most states will probably be rather small. The compliance cost, however, is likely to be substantial, since it requires detailed records of activities in and shipments into a large number of states (whose information requirements differ radically from state to state), preparation of state income tax returns (many of which are more complex than the federal income tax return) and keeping abreast of the constantly-changing tax legislation of an expanding number of taxing jurisdictions. It is this problem —the problem of compliance cost— which Justice Frankfurter emphasized in his dissenting opinion in the *Northwestern-Stockham* case. He aptly pointed out that it is this compliance cost, rather than the tax cost, which as a practical matter may well impose an undue burden on interstate commerce.

Many thousands of businesses have conducted operations in interstate commerce for many years without filing tax returns (or paying tax) in the states in which they have operated. Some (not all) of these states have now indicated that they intend to impose taxes, together with penalties and interest, retroactively on such businesses when they discover them, on the ground that the Supreme Court has now expounded what the law was all along; and that these businesses which failed to comply took a calculated risk in not filing tax returns or paying taxes from the time that they commenced business in those states. This creates a pretty dilemma for such companies—and for their professional advisors. Is it better for a business to go to each state's taxing authorities voluntarily, and attempt to work out a reasonable compromise of prior years' taxes, or is it better to continue business as in the past in the hope that (a) the company won't get "caught" or (b) if the company is detected, a good settlement can be made? Obviously, each business must decide this for itself, but it is appropriate to point out that it is usually possible for the professional advisor of a business to discuss the problem with state tax authorities without disclosing the name of his client, and frequently a taxpayer who makes a voluntary disclosure can obtain a better settlement than someone who waits until presented with a demand by the state. In addition, the increasing exchange of information among the states (and between the states and the Internal Revenue Service) makes it less likely that a taxpayer may in the future do much business in a state for very long without detection.

Possibility of Federal Action—Under the United States Constitution, Congress has the power to regulate interstate commerce. It would be proper, therefore, for Congress to prescribe limitations on and standards for state income taxation of interstate commerce, and certain steps in that direction have already been taken. In April and May of this year, the Senate Small Business Committee held public hearings on the problems created for business by

the *Northwestern-Stockham* decision, and on June 26th the Committee issued a report calling for legislation to limit the power of the states to tax income derived in interstate commerce, and recommending the establishment of a commission to study the problem. Thereafter, Senator Sparkman, chairman of the Senate Small Business Committee, introduced a joint resolution in the Senate providing that until February 1, 1961, no state "shall impose a tax upon the income of any business engaged in interstate commerce for any taxable year unless, during such year, such business has maintained a stock of goods, an office, warehouse, or other place of business in such state or has had an officer, agent, or representative who has maintained an office or other place of business in such state." In the interim, a five man Commission, to be appointed by the President, would investigate the problem and make recommendations to Congress for permanent legislation to provide uniformity and certainty in state taxation of interstate commerce.

The House of Representatives has also shown an awareness of the problem by establishing a subcommittee of the House Judiciary Committee to study the question and make recommendations.

Understandably, perhaps, the tax administrators of the various states have expressed opposition to federal action, claiming that the states themselves will, if given time, adopt uniform rules governing taxability and apportionment of income. It is questionable, however, that such a result may ever be voluntarily achieved, because of economic differences among the states. Manufacturing states, for example, tend to view the place of origin of goods as the place where income is earned, while consuming states place emphasis on the destination of the goods.

Whether Congress will prescribe federal rules remains to be seen. It is questionable in any event, however, that there will be federal action this year, and any Congressional rules which do develop are expected to be prospective in nature, so that businessmen will at this year end be faced with the question of a potential tax liability for past years and the current year. Certified public accountants may also be faced with a ticklish problem in the examination of financial statements—whether it is necessary to recognize in the financial statements themselves or in a footnote a potential liability for current and prior years' state income taxes. It may be necessary to perform an inordinate amount of work to be able to form some opinion of the amount which may be involved. It is more than likely that the lack of accounting records necessary for an apportionment of income will make such a determination a very difficult task.

Accountants will do well to begin to consider that problem now, along with the question of what to say when the client asks, "What shall we do?"

THE MEMBERS SPEAK

By Dale V. Heinbuch

Communication between two people is sometimes difficult and the problems seem to increase at a pace all out of proportion with a greater number of persons. The Illinois Society of Certified Public Accountants has approximately 2,800 members who, while they are banded together in the common cause of promoting Certified Public Accountancy, have diverse interests caused by the size of the firm they are associated with, geographical location, and/or affiliation with industry, government, or educational institutions.

In an effort to maintain and stimulate interest in the over-all common cause, the Society for many years has published a house organ, *The Newsletter*, and a technical magazine, *The Illinois Certified Public Accountant*. The *Newsletter* has been issued on an irregular basis eight to nine times a year while the technical magazine has been issued quarterly. The *Newsletter* is designed to communicate news of current activities of the Society and its members while the magazine is utilized as an educational medium to provoke interest and thought on current problems of practice and theory in the profession.

Because of ever-present budgetary problems, the Board of Directors is constantly assessing the effectiveness of the various activities of the Society in relation to the cost of the programs. In accordance with this practice, the Board requested the Committee on Public Service and Information to review the publications and recommend to the Board any necessary action with respect thereto.

The Committee, in response to the request of the Board, decided to make a survey of the members' preferences regarding the regular publications of the Society and to base its recommendations to the Board on the expressed desires of the membership. A publications sub-committee was appointed to prepare a publications questionnaire, interpret the responses, and draft a report for submission to the Board of Directors.

In December, 1958 a publications questionnaire was mailed to the entire membership. Responses were received from 1,151 or 41% of the members. This rate of response to the questionnaire is phenomenal and indicates a high degree of interest by the members in the publications of the Society. After analysis of the returned questionnaires, the Committee concluded that they constituted a representative sample of the membership.

The Questionnaire

The questionnaire was designed to facilitate tabulation of the responses by geographical area, by type of professional affiliation, by status in public accounting, and by degree of activity

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Dale V. Heinbuch has prepared and submitted this article on behalf of the Illinois Society's Committee on Public Service and Information of which he is a member. Mr. Heinbuch is associated with the firm of Haskins and Sells, Chicago.

in Society affairs. Analysis of these factors would reveal any bias in the questionnaires returned. The questionnaire contained sections designed to determine the relative popularity of *The Illinois Certified Public Accountant* as a technical magazine, the degree of readership penetration, the uses to which the magazine was put, the acceptability of the publication schedule, and the main topics of interest to the readers. A section designed to reflect the popularity of *The Newsletter* was also included. Thus, the questionnaires returned contained indications of the readership acceptance of the present publications and of the areas which should be emphasized to increase their popularity if publication is to continue.

Summary of Responses

Responses from the Chicago area represented 78.5% of the total members responding and 49.4% of this total were affiliated with local public accounting firms, 22% were with national firms, and 28.6% were not in public practice. These percentages correspond very closely with a test tabulation of the membership roster. Of the members in public practice, 24.4% were individual practitioners, 44.1% were partners, 11% were principal-managers, and 20.5% were staff members. Of this total, 32.1% are serving or have served on Society or chapter committees or the Board of Directors, 17.5% attend meetings but do not serve on committees, and 50.4% are seldom able to participate in society activities. Of the last group, a total of 5% is apparently from out-of-state.

One section of the questionnaire was designed to measure the popularity of the technical magazine as compared to similar publications generally available to the members. The *Journal of Accountancy* was the most popular technical magazine with 89.8% of the members indicating interest while *The Illinois Certified Public Accountant* was second with 74% indicating interest. The latter magazine had more readership interest than the next two lower ranked publications combined and, in addition, had as much readership interest as four out of the other five technical publications included in the questionnaire.

The fact that 74% of the members indicate interest and apparently read the technical magazine is not the only measure of its value. To try to determine the degree of readership, sections in the questionnaire asked specific questions about a recent issue of the magazine and how thoroughly it was read. The level of penetration of *The Illinois Certified Public Accountant* is indicated by the fact that 9.1% always read the magazine, 22.2% of the members had read the least read article in the Autumn, 1958 issue, and 49.1% had read the "President's Letter." Also, only 9.8% of the members seldom or never read the magazine, while 45.5% include it in their libraries as a reference tool.

In the Committee's consideration of the publication problem, it was decided to survey the members' reading preferences so that, if the members desired the magazine to be continued, the content could be tailored to fit the wishes of the majority. The greatest interest was expressed in Federal taxes (61.3%), accounting procedures (56.6%), matters of local interest (51.5%), management advisory services (47.8%), and auditing standards (41.8%). Of the remaining six subject matters listed in the questionnaire, 30% or less expressed an inter-

est in them, thus indicating that they are not of major interest at present.

The Illinois Certified Public Accountant is published quarterly and 92.9% of the members believe that it should be continued on a scheduled basis, with 80.5% being in favor of continued quarterly publication. Only 4.8% of the members favored discontinuing publication. The indications are that *The Newsletter* does not have quite the readership acceptance that the magazine has but only 8.8% favor discontinuing *The Newsletter* and the members favor continuing the two as separate publications by over a two to one majority (57.3% to 26.3%).

Variations from Average of Responses

The data in the questionnaires returned to the Committee were transferred to punch cards and detailed analyses prepared of the responses of members by geographical area, type of professional affiliation, status in the profession, and degree of activity in Society affairs. No significant variations from over-all averages were revealed but a few interesting variations appeared.

The Directors and past and present members of committees who responded (369) evidenced a number of variations from the over-all averages. While they are more interested in the *Journal of Accountancy* than the average, their interest in *The Illinois Certified Public Accountant* is equal to the average and only 1.9% favor discontinuance of the magazine compared to the average of 4.8%. They express a great interest in *The Newsletter,* perhaps because their names appear in it rather frequently; however, in contrast, they favor discontinuing *The Newsletter* more than the average. As a group, they favor continuing *The Illinois Certified Public Accountant* and *The Newsletter* as separate publications more than the average.

Interest among members associated with national firms was less than the average in taxes, management advisory services, and practice management and they, as a group, favor discontinuance of *The Illinois Certified Public Accountant* approximately twice as frequently as the average. This is apparently the result of greater specialization in those firms. However, they appear to be greatly interested in the maintenance and promulgation of auditing standards thus indicating that this is a most important duty of the Society.

Members who are active to the extent of attending meetings read *The Illinois Certified Public Accountant* to a greater extent (83.6%) than the average of 74% and apparently comprise a large segment of the readers who regard the magazine favorably. As a group, a larger per cent read the magazine thoroughly than the average and fewer of them think it should be discountinued. In contrast, only 5.5% of this group save the magazine for future reference compared to the average of 45.5% and eliminating the group from the 1,151 responses raises the average to 54%. The group also finds *The Newsletter* of greater interest than the average and does not favor discontinuance.

The responses from inactive members represented 50.4% of the total. The interests of this group correspond very closely to those of active members except that a much greater interest was expressed in articles on Federal taxes, probably heavily weighted by corporate accountants and individual practitioners. They also agree with active members about the publication schedule of *The Illi-*

nois Certified Public Accountant although they are not as interested in the magazine as the average. Their reaction to *The Newsletter* is not as favorable as the average with 11.9% seldom or never reading it. They are in favor of continuing both publications and, if a choice had to be made, would favor continuing the magazine and dropping *The Newsletter*.

It should again be emphasized that the extent of the variations from the over-all averages was not great among the various groups of members. Most of the variations are in the range of plus or minus 4%, there being only two exceptions which were pointed out in the preceding paragraphs. This apparent unanimity among the members was surprising since the responses were put on punch cards in anticipation of wide variations because of geographical and affiliation differences. From this it can be concluded that the members' goals are fairly uniform but the methods used to achieve them often cause the differences of opinion that arise in the Society.

Conclusion

The Committee on Public Service & Information has submitted a report to the Board of Directors of The Illinois Society of Certified Public Accountants containing recommendations relating to the two publications which, in a large part, were based upon the results of the publications questionnaire. Detailed analyses of the data included in the questionnaires were included with the recommendations. This report was approved "in principle" by the Board of Directors on May 25 and is presently under further consideration.

Opportunities For Broader Management Services

(Continued from page 23)

that public accountants can render to the managements of individual enterprises.

This paper has presented the broad framework of some of the major general management areas in which public accountants can work in concert with an enterprise management to improve the overall planning and control of an enterprise's activities. These areas are: (i) refining and improving the environment and the machinery for formulating enterprise policies and plans, (ii) developing relatively ideal continuous analysis and forecast of long range consumer demand, and (iii) improving the internal communication system of the enterprise.

Too often the sphere and contribution of public accountants have been viewed from the narrow confines of technical accounting. The writer believes the time more than ripe for enterprise managements to transcend using their independent accountants as mere "fact finders and reporters" and to use them more effectively as ancillaries in the highly productive areas of management planning, decision making, and communication of enterprise policies.

WHY NOT THE NATURAL BUSINESS YEAR?

Prepared by the
Illinois Society Committee on Natural Business Year

In the public practice of every CPA, the $64.00 question has always been—"Why do so many businesses still close their books on the basis of a calendar year, when a closing coinciding with their natural business year offers so many advantages?" As many of us know, it is sometimes just about as difficult to get management interested in changing a calendar year corporation to a fiscal year as it is to attempt to convince a man to change his religion or politics. So we certified public accountants must be dynamic salesmen, constantly preaching the gospel of the natural business year. This article, then, is primarily aimed at furnishing practicing accountants with some ammunition for use in our cold war against the continuance of calendar year reporting by many of our clients.

The average businessman, when hearing the natural business year mentioned, will usually admit having heard about it at one time or another. However, when pressed further as to whether or not he utilizes it for his business, in many instances he will answer you with a barrage of defensive statements, which may be summarized as follows:

(1) The Internal Revenue Service frowns upon changing taxable years.
(2) Financial reports will no longer be comparative with other years.
(3) Why should I use a fiscal year when no one else seems to use one?
(4) How will I be able to compare my results with my competitors, who remain on a calendar year?
(5) (Desperation clincher) The fiscal year idea sounds good, but isn't it really a device CPAs use to facilitate the spreading of their work load so they can accept more clients?

Some of us might be happy to retreat after a defense such as this. But if each argument is analyzed clearly, it can be reasonably answered and defeated. Don't let your clients side-step your suggestion with any of these old chestnuts, because they just won't hold water under close scrutiny. Let us disprove them one at a time, in the same order listed above.

Number One—"The Internal Revenue Service frowns upon changing taxable years." This is simply not true, particularly for corporations. Reg. 1.442-1 (c) allows corporations to change their year *without advance permission* if they have not changed their tax year in the previous ten years, there is no operating loss in the short year period between the two closing dates, the taxable income for the short period is, when annualized, at least 80% of the taxable income for the preceding year, and other minor technical requirements are met. However, in cases where prior approval is needed because of failure to meet one of the aforementioned requirements, a strong business purpose must be demonstrated. The natural business

year is acceptable as such a purpose. A word of warning might be appropriate here. If the short period is one resulting in an operating loss, permission to change years may well be denied no matter how strong a business reason the corporation might have for requesting the year change. Partnership year changes are a bit more difficult and are allowed without the Commissioner's prior consent only if all of the principal partners (interests of 5% or more) have the same taxable year to which the partnership changes. [Reg. 1.442-1(b)(2)]. From the foregoing, it appears the Internal Revenue Service is not against the idea of changing taxable years, and in fact encourages changes to a natural business year.

Number Two—"Financial reports will no longer be comparative." This may not appear to be much of an argument to anyone with an accounting background, but to many businessmen it may well loom as insurmountable. Accountants should show their clients that it is possible, in most instances, to prepare comparative figures which will be suitable for management purposes without an undue amount of effort. In other words, figures for the prior period usually may be restated so that they cover a period that is comparable to the short year period of change. Also, the comparative statements applicable to the first twelve month year after the change will require restatement. The accountant should indicate the fact that the benefits of having the complete picture of a full operating cycle will more than outweigh this additional effort of recasting figures for comparison purposes. Internal records require no significant changes, and the year-end closing work, because of reduced inventory and general slowdown, will require less effort to complete.

Number Three—"No one else is on a fiscal basis." This fallacy is best demonstrated by citing the most current figures available from the Internal Revenue Service on the number of corporate tax returns filed on the basis of fiscal years. The figures show that for tax years through June, 1956, 48% of the corporate returns were on a fiscal basis, as compared with 1930 when the percentage was only 13%. This is an increase of almost 300% in 26 years. Actually, we anticipate that it will not be long until the number of corporations filing on a calendar year basis will be in the minority, so how can anyone still contend that: "No one else seems to use a fiscal year"?

Number Four—"I would be unable to compare my operations with competitors remaining on a calendar year." As in argument number two, this is a matter of recasting your figures to a comparable basis for management purposes. This is not an uncommon procedure. As the above mentioned percentages disclose that more and more businesses are changing to the natural business year, it will eventually be the calendar year corporation that will be required to recast figures in order to be comparative with fiscal year competitors.

Number Five—"The natural business year is merely the CPA's method of spreading his work load." Let us be honest and admit that the CPA does benefit from fiscal year closings of his clients. Its universal use would do much to assist him in keeping a steady staff of competent employees and also permit additional interim work. However, the benefits derived by the CPA, which after all flow

eventually to his clients, are small in relation to what the businessman gains.

What are these benefits the businessman gains through use of a natural year? We are certain that all accountants know them, but let's review and re-emphasize them. The list below summarizes some of the principal benefits derived through the use of the natural business year. This is not intended as an all-inclusive list of benefits. Many of you will have some of your own to add, peculiar to individual businesses or industries, or caused by geographic locations (i.e., physical inventory taking in severe weather, etc.).

(1) The balance sheet will usually present the company's most liquid position—frequently a help in getting bank credit.
(2) The income statement will cover one complete business cycle—rather than a mixture of the end of one season and the beginning of another.
(3) A fiscal year avoids confusion with calendar year-end activities, payroll tax returns, etc.
(4) Inventory can be taken when it is lowest and when employees are least busy.
(5) Financial statements for each year should be available earlier.
(6) Income tax returns will show smaller amounts for inventories and accounts receivable, thereby reducing the area of possible dispute with the government.

Item four alone should cause the average small corporation to consider how much of a saving can be effected by use of the natural business year. Obviously it is preferable to shut down a plant when taking a complete physical inventory. Such a stop in production during the peak season, coupled with the cost of the men assigned to take the inventory, can be a very costly procedure. Therefore, it is simply good logic to take inventory when it is at its lowest level, and when the loss of production caused by the shut-down will be least harmful. If the natural business year will promote this saving, can the average businessman afford to ignore its uses and benefits?

A further point to consider when discussing the use of fiscal years with clients is the option new corporations have to adopt in their first return a fiscal year without Treasury Department advance approval. (Reg. 1.441-1). Our committee has in the past conducted an informative campaign in this respect through contacting incorporators of new corporations. We believe this is an important element to be considered in planning for new corporations, which is sometimes unknown or overlooked by the incorporators.

The natural business year of an enterprise has been defined as a period of twelve consecutive months, or thirteen periods, ending when its activities have reached the lowest point in its annual cycle. This means that inventories, accounts receivable and payable, and bank loans, if any, have all been reduced to their annual minimum. We believe that all accountants are familiar with this definition, but are our clients also just as familiar with its meaning? It is up to us to see that they are, because, in the final analysis, the natural business year doctrine is spread most effectively at the "grass roots" level.

REIMBURSED EXPENSES

By James E. Burgess

Introduction

The advance publication in October, 1957 of the Federal individual income tax return for that year contained a new line entitled, "6(a) Travel, Reimbursed Expenses, etc." This seemingly innocent line created a furor among business people and taxpayers that literally rocked the foundations of the Internal Revenue Service. Reeling under the attack led principally by the public press the Service in a news release on November 11, 1957 tried to temper the rising tide of indignation and stated, in part, ". . . The new line will enable the Service to give attention to those returns where deductions for expenses appear to be disproportionate in relation to the employee's income and occupation, and thus aid in detection of abuses that have risen in this area. . . ." This merely fanned the fires already raging in the hearts of expense-conscious taxpayers, and finally on November 25, 1957 the Service announced that taxpayers would not be required to answer line 6(a) of the 1957 return. The reason given for this decision was that most employees who received reimbursement turned over bills and receipts to employers and to reobtain this data so late in the year would place an undue burden on many taxpayers. However, as a parting volley, the Service announced that all individual taxpayers who incur expenses in connection with their employment should keep adequate records of their expenditures and reimbursements so that for 1958 and later years they will be in a position to supply expense account information from their own personal records.

Everyone realized that this was but a temporary withdrawal and that the problem of expense account reporting was still not solved. The Service was also cognizant of this and took upon itself to issue regulations on this particular subject which would at least let every taxpayer know the Government's position. Accordingly, proposed regulations on "Reporting and substantiation of traveling and other business expenses of employees" were issued on March 12, 1958 and final regulations (Regs. 1.162-17) on the same subject became effective on August 28, 1959.

Expense Account Scrutiny Prior to 1958

Actually the 1957 announcements should not have caused the taxpayer reaction that it did. For the past six years the Service has shown in various announcements that it was thoroughly familiar with the many abuses that actually existed in the expense account area. It was announced in 1952 that special attention was to be given to examination of large entertainment expense deductions and further indi-

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cated that full substantiation would be required. This program did not prove too satisfactory and in 1954 the Service issued further announcements[1] in an effort to expand the scope of investigation and set forth the degree of substantiation required. These pronouncements, plus proddings from superiors, caused field agents to become considerably tougher in the expense account area. In 1957 a further release[2] directed agents to continue their close review of club dues, entertainment, travel, and maintenance of automobiles, yachts and company-owned residences. Close attention was to be directed to branch offices in resort cities established for the purpose of sending business executives there for vacations. Other areas to be closely scrutinized were hunting trips, sporting events in distant cities and the like, all attended by hard-working executives because business expediency demanded their presence.

All of this indicated much activity by the Service and taxpayers were feeling the harsh results but still no adequate regulations were in existence that could serve as a general guide. The late 1957 controversy changed this. We now have some ground rules to follow, but only time will tell how helpful they will be.

Expenses Now Fall Into Two Classes

Basically, the new regulations categorize expenses into two classes; the first being those for which the employee *is* required to account to his employer, and the second, those expenses for which the employee *is not* required to account to his employer. An employee is considered as having accounted when an expense report is submitted which shows "the business nature and amount of all the employee's expenses (including those charged directly or indirectly to the employer through credit cards or otherwise) broken down into such broad categories as transportation, meals, and lodging while away from home overnight, entertainment expenses, and other business expenses."

Mileage Allowance and Per Diem

Many companies as a matter of policy reimburse employees at a flat mileage allowance for business use of their personal car and on a per diem basis for certain other expenses. In these situations the Regulations state that the Commissioner, in his discretion, may approve reasonable business practices under which mileage and per diem in lieu of subsistence and similar allowances providing for ordinary and necessary business expenses in accordance with a fixed scale, may be regarded as equivalent to an accounting to the employer.

Further information on this subject was contained in a recent ruling[3] in which information was requested as to the circumstances under which mileage and per diem allowances would come under the reasonable business practice criteria as set forth in the Regulations. As the result of a study on this particular subject, the Commissioner determined that an employee who incurs ordinary and necessary business expenses for travel (including meals and lodging) and transportation for which he is paid a fixed mileage allowance or a per diem allowance by his employer in lieu of subsistence will be deemed to have "accounted" to his employer for such expenses if the mileage and per diem

[1] Rev. Rulings 54-195, 1954-2 CB 47; and 54-497, 1954-2 CB 74.

[2] IR Circular No. 57-85, June 20, 1957.

[3] Rev. Ruling 58-453, 1958 CB 37.

rates are not in excess of 125% of the rates authorized to be paid by the Federal Government in the locality in which the travel is performed. For information purposes, the Federal Government figures were merely used as a norm and within the Continental United States they pay 10 cents per mile for auto allowance and $12 per day for the per diem allowance in lieu of subsistence. Therefore, under this ruling an employee will have "accounted" when his mileage and per diem allowances are not in excess of 12½ cents per mile and $15 per day, respectively. It would appear that in situations of this type if the expenses are less than the reimbursements only the excess need be reported.

Procedure When "Accounting" Is Required

Where the employee is required to "account" to his employer for travel, entertainment expenses and the like, reporting for Federal tax purposes will not be required if the reimbursement equals the expenses. The term "reimbursement" includes all direct or indirect charges to the employer for which the employee receives payment in the form of advances, use of credit cards, or exact reimbursement on a periodic basis. A statement appears on the 1958 tax return for taxpayers to check if they "accounted" to their employers and reimbursements did not exceed expenses.

Exceptions will occur (1) if the reimbursements exceed expenses in which event the excess must be included as income and reported as such on the return; or (2) if the expenses exceed reimbursements, the taxpayer may elect not to claim the excess in which event he will merely indicate that reimbursements did not exceed expenses. If the employee desires to deduct the excess expense he will then follow the procedure to be used by employees who are not required to "account."

Procedure When "Accounting" Is Not Required

An employee who is not required to "account" to his employer must include the following information on his return:

1. The total of all advances, reimbursements (including credit and charges) received from the employer.
2. The nature of the employee's occupation and number of days away from home (overnight) on business.
3. The total amount of business expenses incurred by the employee, segregated into broad categories, such as transportation, meals, lodging, entertainment, and other appropriate items.

Information Returns by Employer

Employers are not required to submit Form 1099's with respect to payments made in reimbursement of expense when the employer requires an "accounting." When an employee is not required to "account" then a Form 1099 must be submitted by the employer.

Unusual Situation

It is entirely possible for the same employee and employer to use various methods of expense reporting. For example, a salesman travels for approximately ten months each year in a particular state. He is reimbursed on the basis of actual expenditures which are submitted to the employer through a weekly expense report. It would appear that this salesman has "accounted" and if the reimburse-

nents equal the expenses no reporting s required by the salesman and the employer is not required to submit an information return.

Let us further complicate this example by assuming that in the other two months the salesman goes on buying trips to distant cities. On these trips the salesman is given a per diem allowance of $20.00 per day. Since this daily allowance is in excess of that allowed by Revenue Ruling 58.453, the salesman does not "account" to his employer so he would be required to include all of the per diem allowances less applicable expenses in his income tax return. The employer should submit a Form 1099 and only report the per diem allowances. It would not appear that the expenses incurred where the employee was deemed to have "accounted" would have to be reported by either the employee or the employer. This split reporting can obviously create bookkeeping complications. It would appear in the above situation that the expense account procedures should be revised so that the employee and the employer would both be relieved of the responsibility of reporting.

Taxpayer's Responsibility for Substantiation

The Regulations state that any taxpayer may be required to substantiate information concerning expense accounts as may be necessary to properly determine tax liability. Ordinarily taxpayers will not be called upon to substantiate this information except those that fall into the following categories:

1. A taxpayer who was not required to "account" to his employer or who does not "account."
2. A taxpayer whose expenses exceed the total of amounts charged to his employer and amounts received through advances, reimbursements, or otherwise and who claims a deduction on his return for such excess.
3. A taxpayer who is related to his employer within the meaning of Section 267(b) of the 1954 Internal Revenue Code.
4. Other taxpayers in cases where it is determined that the accounting procedures used by the employer for the reporting and substantiation of expenses are not adequate.

These pronouncements certainly indicate that in the final analysis the Service will look to the particular employee for substantiation. However, it would appear that many employees will be removed from close scrutiny, especially when the reimbursements are equal to expenses and the employee is a non-stockholder or minority stockholder. However, if the employer's records are inadequate from an internal control point of view, even a non-stockholder employee may be required to substantiate expenses so as to eliminate the possibility of tax-free income being received by the employee under the guise of a business deduction to the employer.

Stockholder Employees

The area which appears to be ripe for special attack is where an employee is directly or indirectly more than a 50% stockholder. The indirect category would include stock owned by brothers, sisters, husband or wife, ancestors, and lineal descendants. Thus, if John Jones owned only 30% of the stock of A corporation and his father owned 40% of the stock, the expense reports of John Jones might be subject to close scrutiny because

John Jones and his father owned 70% of the stock of A corporation.

Expense reports of employees in this category will be closely examined even though reimbursements are equal to expenses. The Service feels that the control position of the stockholder employee might enable him to cause the corporation to pay certain entertainment and travel expenses that are not properly ordinary and necessary business expenses and thus inure to the personal benefit of the stockholder employee. When this occasion arises it has been the recent practice of the Service to disallow the deduction to the employer as not being ordinary and necessary to the furtherance of the business and to add the disallowed amount to the income of the individual stockholder employee under the theory that he has received a dividend. In these situations double taxation obviously arises, and in many instances the amount of the total tax, including that of the corporation and the individual, is in excess of the disallowed amount.

Treatment of Stockholder Employees

Many times we, as tax practitioners, are asked if the Government has a right to make these disallowances, and construe taxable income to the individual taxpayer. A recent case [4] probably best illustrates the Government's effectiveness in this regard. Two brothers with other family members owned controlling interest of a corporation. In the year 1952 the brothers incurred approximately $11,000 of travel and entertainment expenses for which they were reimbursed by the corporation. The Service in its examination of the corporation's tax return disallowed 25% of the total amount, or $2,800. The Service further indicated that the $2,800 was to be considered a dividend and taxable as such to the brothers. The Court concurred and stated that the disallowances were proper. It did not question that the moneys had not been spent for business purposes but the lack of adequate substantiation precluded their acceptance of the entire amount. The brothers were unable (or unwilling) to completely furnish the names of persons entertained, the kind of entertainment, or specifically at least the business purpose of the entertainment. The Court further stated that the burden of proof resided upon the taxpayers and, accordingly, it was their obligation to show the nature of the expense item and its purpose. After the disallowances were asserted, the brothers then desired that the corporation be allowed the deduction for additional salaries or other compensation as corporate officers. The Court stated that this was obviously an afterthought, that there was nothing in the record to show that such additional compensation was intended or expected and that the record further fails to support the view that any such amounts when related to the substantial salaries, commissions, and bonuses were reasonable. Other cases with similar facts often have the same result.

Accumulated Earnings Needed To Sustain Dividends

In most situations, where there is a disallowance to the employer and subsequent income to the stockholder employee, the corporate employer will have sufficient accumulated earnings to sustain the position that the employee received a dividend. When

[4] Stanley C. Olson, Buford W. and Demores Olson, Chas. Olson & Sons, Inc., TC Memo 1958-56: April 9, 1958.

accumulated earnings are not present and a disallowance of expenses is made, the stockholder employee has received a non-taxable return of capital.

Avoiding Double Taxation

A possibility for at least avoiding the area of double taxation might be a fixed expense allowance for which the stockholder employee is not required to "account" to the employer. In these situations it should be specifically understood between the employee and the employer as to the nature of the expenditures to be made under an arrangement of this type. A recent Revenue Ruling [5] stated "... that a corporate officer who claims deductions for traveling and entertainment expenses incurred on behalf of the corporation must bear the burden of proof that he is entitled to such deduction . . . a resolution requiring the assumption of such expenses by him would tend to indicate that they are a necessary expense of his office." While it is true that the burden of proof for the expenditures falls upon the corporate officer, nevertheless under current Regulations he still appears to have the burden of proof for expenses even on a reimbursement basis if he owns directly or indirectly more than 50% of the stock of the corporate employer. It would appear that under an arrangement of this nature at least the deduction to the corporation would be safe and any disallowances would result in tax to the corporate officer only. Bear in mind, however, that compensation, expense allowances and other fringe items paid to or for the benefit of the corporate officer must still be considered reasonable in the aggregate.

A case [6] on this subject involved an expense allowance of $6,000 per year, which allowance was approved by the Board of Directors and the resolution further provided that the corporate officer would not be required to render an accounting therefore. The Service in its examination of the corporation's tax return disallowed the $6,000 of expenses and further claimed that the amount was taxable to the officer. The Court agreed with the conclusion that the expense allowance was not reasonably substantiated; however, they stated that it was not substantiated as entertainment expense but did constitute additional compensation to the officer, as his salary plus the expense allowance was not considered excessive. The individual did have taxable income to the extent of $6,000 but double taxation was not involved.

Records to be Kept

This is a subject on which there has been much discussion, but basically it is quite simple. The Service requires taxpayers to maintain as adequate and detailed records of travel, transportation, entertainment, and similar business expenses as practical since the burden of proof is on the taxpayer to show that the expenses were not only paid but that they actually constituted ordinary and necessary business expense. It is suggested that a daily diary be maintained in sufficient detail to readily identify the amounts, the nature of the expenditure, persons entertained, and the business purpose. It is recognized by the Service that documentation of all expenditures is practically impossible. Thus, detailed records of small expendi-

[5] Rev. Ruling 57-502, IRB 1957-43, 15.

[6] W. Horace Williams Company, Inc., DC La. July 10, 1956.

tures, such as tips and the like will not be required.

If the taxpayer does not have a complete record of expenditures and receipts the Service again becomes somewhat realistic in that they may be able to establish the amount of the expenditures by approximations based on secondary sources of information. For example, a taxpayer might spend five or six days in another city. In cases of this nature, rail or plane fares can be determined with a degree of exactness and possibly automobile expenses can be approximated on the basis of mileage covered. Meals and lodging might be computed based on receipted hotel bills or on known hotel rates and living expenses in the particular community. It must be remembered that the burden of proof is on the taxpayer to establish that the amounts claimed as a deduction are reasonably accurate. Due consideration will be given to the reasonableness of the expenditures taking into account the employee's income and nature of his occupation.

Cohan Rule and Its Application

Much publicity has been given to the Cohan rule. This resulted from the case[7] of the famed theatrical producer, George M. Cohan, who spent considerable sums of money in travel and entertainment expenses in the furtherment of his various productions. He was unable to provide adequate documentation of all his expenditures. The Court stated that "Absolute certainty in such matters is usually impossible and is not necessary." It further directed that "the Board (Tax Appeals) makes as close an approximation as it can, bearing heavily, if it chooses, upon the taxpayer whose inexactitude is of his own making." As a result of this decision a certain portion of Mr. Cohan's expenditures, though unsubstantiated, were allowed. This approach has been used many times since 1930 and is generally applied to situations where, in the absence of satisfactory evidence as to claimed expense deductions, the Courts have allowed an approximate reduced amount.

The Cohan rule should not be followed literally for the Courts do require a degree of substantiation. In the case previously referred to where the taxpayer had a $6,000 expense allowance, it was necessary for him to take his own case[8] to Court in an effort to prove his deductions. He was certain that he spent $6,000 or more in paying for food, liquor, and travel for the entertainment of customers but he could not offer any proof. The Court held that in a suit for refund the burden is on the taxpayer to show that the tax was wrongfully collected, and that carries a burden of showing some substantiation that entertainment expenses were actually paid or incurred. Obviously, the refund was denied.

All is not lost however, even if a taxpayer's expenditures are questioned and initially disallowed by the Service. In one case[9] the Government contended along with other reasons that the expenditures should not be allowed because the taxpayer did not carry the book with him and only put in the amounts spent when he returned to the office. The Court took the position that this brief delay did not render the evidence untrustworthy.

[7] George M. Cohan, 39F (2d) 540 (CA-2, 1930).

[8] W. Horace Williams, Sr., CA-5, July 18, 1957.

[9] John P. Wagner, et al., TC Memo 1958-112, June 16, 1958.

Conclusion

Actually, little has changed in the entertainment and travel expense area. The Regulations did define the Government's position and eliminate the Line (6(a) requirement that had originally been proposed for 1957. However, the 6(a) victory might be short-lived as Treasury Under Secretary Fred C. Scribner, Jr., recently stated that: "If the new Regulations don't work, the Service will have no alternative but move promptly to the much more stringent position represented by Line 6(a) which appeared on the 1957 tax return and which we all hope has been permanently put aside for the new approach." If the Service follows the threat posed by Mr. Scribner we will be in the identical position that we were a year ago.

Still unanswered is the question as to whether reimbursements constitute gross income. Some support for their inclusion as such is created by certain wording in Section 62(2)(A) of the 1954 Internal Revenue Code and the Regulations thereunder. It would appear that the Service might be subscribing to this position in light of Mr. Scribner's remark. A possible rebuttal to this contention might be that reimbursements do not constitute taxable income as the employee in spending the money is merely acting as an agent for the employer.

Basically, the Service will still look to individual taxpayers for substantiation but it will do so only under certain specified conditions. Under present Regulations this should have the effect of removing certain taxpayers from close examination and thus enabling the Service to more readily concentrate on classes of taxpayers that have always been the prime target, the large spender and the stockholder employee.

The rules are strict and there are Court decisions to substantiate Service's position. The best advice that can be given is to have adequate documentation of all expenditures wherever practical. Approach the problem on a reasonable basis, and if the Treasury Agents adopt the same attitude everyone should be a lot happier.

BANK ACCOUNTING

By George Richards, Jr.

Introduction

I always remember some advice given me when I first began working as a public accountant. I was employed by a small CPA firm and, after a couple of years of apprenticeship, had reached the status of an "in charge" accountant. Quite frankly, the only person over whom I was "in charge" was myself and, as many of the clients were new to me, I had a certain amount of misgivings about the whole thing.

Like other small firms, we had never quite reached the point where we had written audit programs for many of the smaller engagements. In most cases the only guide was last year's working papers. This raised the problem of what to do first on the audit and, more particularly, the best approach to take in order to avoid any display of fumbling or inexperience in the client's office.

I discussed my problem with a partner of the firm and he told me, "When in doubt, always start by taking a trial balance of the general ledger. Then if you still are uncertain what to do, reconcile the bank accounts and count petty cash. At this point, if you still have doubts on how to proceed, select prepaid insurance or some other relatively common accounting situation for examination. After doing all of these things, if you still don't have your feet on the ground, you might just as well pack up your brief case and come back to the office."

While this is not much of a story, I know from experience that it is pretty good advice. Of course it is significant to note that my small firm employer did not engage in any bank audits. If the foregoing techniques were employed there, I am afraid the results might be disastrous.

If you contemplate performing a bank audit, you must have a working knowledge of the bank's accounting system before you undertake the engagement. There is no implication here that bank accounting is difficult or complicated. The important point is that it is different. You must know what you are doing from the outset. "Control" is the key word. When you walk in the door you have to know immediately how to control assets and accounting records. This involves among other things, of course, a definite understanding of the bank accounting system.

Although the banking industry as a whole does not use a uniform accounting system, there is a certain degree of similarity in accounting methods. In describing bank accounting here I have elected to approach the subject from the standpoint of differences between it and conven-

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tional accounting rather than attempting to give you a detailed explanation of a bank accounting system. I believe that you will agree that this a more practical approach since we will not be spending time discussing accounting procedures that are common to banks and to other organizations and which, for that reason, are already quite familiar to you. We also will want to consider certain general aspects of the classification of accounts in a typical small bank and some of the principal accounting records should be mentioned.

Complete Daily Posting and Trial Balancing

One of the more significant differences between bank accounting and other forms is in the method of posting and trial balancing the general ledger. Because of the fact that banks must prepare a daily statement of condition or balance sheet, it is necessary that the general ledger be posted and trial balanced at the close of each day's business. The bank must be in a position to prepare its financial statements almost immediately after the day's transactions have been recorded.

As a matter of expediency the usual procedure is to net the income and expense accounts since the last closing date and carry this amount in the statement of condition as a suspense balance usually labeled "profit and loss" or some similar designation. This procedure eliminates the need for closing out the income and expense accounts to undivided profits at the end of each day. There is no uniform procedure for closing income and expense accounts to the undivided profits account; however, many banks do this on a semiannual basis and carry the net current earnings figure in the statement of condition in the manner described at times other than the closing dates.

It can be readily appreciated that the need for daily financial statements naturally influences the whole bank accounting system and contributes to other differences that set it apart from conventional accounting. For example, banks do not use accrual accounting as we know it. The need for preparing financial statements on such an immediate basis makes it impracticable to hold the books open for periods long enough to establish all expense and income accruals. Some banks speak of the fact that they use accrual accounting, but upon closer analysis it will become apparent that accrual methods are applied to certain income and expense accounts but are not extended to many other areas.

Preponderance of Balance Sheet Transactions

In the majority of conventional accounting systems we find many transactions that affect both income statement and balance sheet. For example, recording sales, incurring expenses, and the like, result in simultaneous changes in both income and balance sheet accounts. While some transactions pertain to balance sheet accounts only, the proportionate number of these in relation to other entries is not particularly significant. In bank accounting the situation is quite different. The majority of daily transactions affect only balance sheet accounts. To give you some idea of the volume of transactions of this nature, it is not uncommon for a small bank (and by small we mean one having deposits of $10,000,000 or less) to handle 4,000 or 5,000 items a day—each one of these being an accounting

entry affecting a balance sheet account. This difference in accounting influences the system that a bank must follow, as methods must be devised to expedite the sorting and summarization of such a volume of accounting entries. When we consider the tremendous volume of individual transactions, we begin to appreciate the need for high speed methods of classifying this accounting information.

Importance of Accountability Between Individuals and Departments

The importance of internal control and the establishment of individual accountability cannot be over-emphasized in banks. When we consider that each department and the individuals working therein handle large amounts of cash and other negotiable items such as checks, notes, and securities, we can readily understand the need for proper controls to establish accountability. Accountability between individuals and departments is usually controlled through the use of "blotters" or "proof sheets" and the use of a system of departmental or individual transfers. For example, if a batch of checks is transferred from one department to another for further processing, the total of the items is charged to the department receiving them and offset by a credit entered on the department proof sheet of the department sending the items. These departmental debit and credit transfer amounts "wash-out" at the end of each day. In effect, since they exactly offset one another, they can be eliminated from general ledger posting.

Another reason why individual accountability must be maintained in a bank is the fact that transactions and accounting entries are continuously flowing from one individual or department to another. For example, a teller cashes a check drawn on a New York bank, the money is paid to the customer, and the check is placed in the teller's drawer. He does not wait until the end of the day for further processing of the item as this would create a bottleneck if all transactions were handled in this manner. Several times a day he will total the checks cashed and transfer these items to another department. He will charge this department with the total of such items and, in turn, the department will credit him. The check which he has just cashed on a New York bank will probably not stay in his cash drawer more than a couple of hours. It will then be sent to the central proof department where, along with other items, it will be sorted, listed, and proved for further processing. As we are talking about an out-of-town item, this check will be forwarded to the transit department, where it will be listed in a "cash letter" and probably sent airmail to a New York bank that acts as correspondent for the cashing bank. It is quite possible that this check will actually leave the bank before the close of business the day received. The important point brought out by this illustration is the continuous movement of items in the bank. Each individual (or department) performs certain functions with respect to the items that he handles and then passes the items along for further processing. This is why accountability must be maintained at all times.

Extensive Use of Cash–Basis Accounting

We have already mentioned that there are practical considerations that

influence the bank's use of cash-basis accounting. The importance of timely preparation of financial statements determines this, although there are other contributing factors. Most transactions arise in banks as a result of receipt or payment of cash. This fact has led to the use of entry tickets which record the offset to the cash side of each transaction. For example, when a cash deposit is made at a teller's window, the cash is placed in the teller's drawer and the deposit ticket along with others becomes the basis of a general ledger credit entry. Thus, in banking we find that while double-entry accounting is used, the recording processes are geared to summarize the non-cash side of accounting entries. This is done through the use of single-entry tickets.

This brings to light another significant difference in bank accounting: that is, the absence of conventional journals. Time would not permit the recording of each transaction in a columnar journal and posting the journal column totals to the general ledger. A faster method must be employed to summarize and record daily transactions. Thus, we use entry tickets in place of journals. Once the equality of debit and credit amounts is established, the tickets are sorted and classified for the purpose of summary posting.

This general procedure is applied to all accounts except cash. The cash balance in the teller's drawer changes with each transaction and, at the end of the business day, the net change in cash should equal the net debits and credits to other general ledger accounts. This brings up another peculiarity of bank accounting in the posting of the general ledger. All accounts of the general ledger are posted to give effect to the day's transactions except the cash account. The cash account is cleared each day of the opening balance and the new balance at the close of business is entered as a debit. All other things being equal, this procedure should result in the general ledger being in balance after the posting of all transactions.

Classification of Accounts and Certain Accounting Practices in Banks

Unquestionably we can spend a lot of time reviewing the classification of accounts in the bank's general ledger for purposes of explaining account functions. However, this seems hardly necessary as the nature and purpose of many of the general ledger accounts are self-evident. In the interest of conserving time it seems more appropriate to restrict our discussion to account classifications and practices peculiar to the industry and, in themselves, somewhat foreign when compared with other types of business activity.

The concept of working capital has no special significance in the financial management of a bank. In fact, banking has a complete set of its own rules; thus, there is no division in this classification of accounts for current assets or current liabilities. In lieu of this, account groupings are somewhat as follows. The assets are usually arranged in order of their cash availability, although occasionally there are some exceptions to this method of presentation. Generally, assets can be divided into five groups:

First we have cash and balances due from other banks. Cash consists of total balances of teller funds and vault reserves plus checks and other items in process of collection. Bal-

ances due from other banks represent deposits with correspondents used to facilitate check collection and other banking services. "Due from" accounts reflect transactions initiated by the bank maintaining such deposits and are not customarily used to record transactions originating in the depositary institutions. "Due to" accounts are for the latter purpose and it is not uncommon to find reciprocal balances in the statement of condition representing accounts with another bank.

The second group of assets is that of investment securities, sometimes referred to as the bank's "secondary reserve." These, for the most part, are United States Government obligations. The balance includes "nontaxables" consisting of state, county, and municipal securities, and some banks have modest investments in taxable issues of corporations, railroad trust certificates, and other debt securities. It is significant to note that, with certain exceptions, banks are not permitted to invest in common stocks. Federal Reserve members are required to subscribe to shares of capital stock in the Federal Reserve Bank of their district equal to a percentage of their own capital stock and surplus accounts. In Illinois quite a few banks carry stock investments in subsidiary companies that conduct safe deposit operations on the bank premises. Also, recently a trend has developed for financing new quarters through subsidiary building corporations.

The third division of assets pertains to loans. Time does not permit a detailed analysis of the many types of loans that a banking institution makes; however, loans usually can be divided into three categories. These consist of first mortgage loans on real estate, consumer credit loans, and commercial loans. Separate accounting records are maintained for each of these categories. It is significant to note that banks are not permitted to make so-called "capital loans" and, for this reason, commercial loans are concentrated on seasonal financing of business transactions except to the extent of collateralized obligations and certain other exceptions.

The fourth asset subdivision relates to physical properties used in connection with banking operations. These consist of bank premises, furniture and equipment, etc. Many banks follow conventional accounting practices with regard to depreciation and capitalization of fixed assets. However, there still remain a number of banks that follow arbitrary accounting practices with respect to fixed assets. Thus we find situations where items that, under generally accepted accounting principles should be capitalized, are written off at the time of acquisition and depreciation policies are often arbitrary and are influenced by a desire on the part of management to reflect a certain end-result in earnings.

The final division of assets is a "catch all" for items that cannot be properly classified under the first four divisions mentioned. Here we find prepaid insurance, sundry accounts receivable, interest earned but not collected, and other items. The total of other assets is never material and often is less than 1%.

No hard and fast rule can be given for the dollar distribution of the banks assets although it is worthwhile to note that for 1958 the distribution of assets of member banks of the 7th Federal Reserve District showed the following average percentages:

Cash assets	18.5%
Investment securities	46.5
Loans	34
Real estate and other assets	1

One other point of significance in analyzing the assets of a bank is that considerable importance is attached to the term "risk assets." These are the total assets reduced by cash assets and investment in United States Government securities. The ratio of risk assets to capital is an important yardstick in measuring the relative strength of the bank. While there are many other ratios that could be discussed, this one is mentioned in particular because of its importance.

The classification of liabilities in bank accounting is quite different from conventional practice. Liabilities can be subdivided into the following categories: deposits, other liabilities, and net worth accounts. Deposits are classified as "time" and "demand." Regulation Q of the Board of Governors of the Federal Reserve System provides a definition for each type of deposit. Generally, time deposits represent liabilities that are not immediately payable and for which the bank reserves the right to require notice before withdrawal can be made. These deposits usually bear interest and consist of savings accounts, time certificates of deposit, and time deposit open accounts. It should be mentioned that demand deposits not only include commercial and individual checking accounts, but also the bank's liability for official checks and other obligations outstanding.

Other liabilities in the classification of accounts consist of accruals for taxes, interest on time deposits, and other obligations arising from operations that the bank considers expedient to reflect in the accounts on an incurred basis. We have already mentioned that banks do not reflect all accruals in their financial statements because of the timely basis on which financial statements are prepared.

The net worth accounts consisting of capital stock, surplus, undivided profits and appropriated reserves are the subject of special comments in later paragraphs. For present purposes they are identified only as the third subdivision of liabilities.

No particular purpose would be served by a lengthy discussion of the various income and expense accounts since they are more or less self-explanatory. The principal earning assets of investments and loans generate interest income which is usually segregated into taxable and nontaxable elements to facilitate preparation of tax returns. Other incomes for which accounts are provided consist of service charges, exchange fees, safe deposit rents, etc. In the expense account classification section the most significant account is that of salaries which represents approximately one-third of the total expenses of operation. Interest costs are also a substantial item for which expense accounts are provided; however, other categories represent relatively nominal items and would not be too much different from what you would anticipate in any other service organization.

Check Collection System

We are all aware of the fact that most business transactions today are settled by check and that the banking system has the responsibility of check collection. Checks received by a bank for collection can be roughly divided into three categories. First we have "on-us" checks. These items are

drawn on accounts of the bank receiving them and at the close of the day will be charged against such accounts and in this manner collected. The second category is that of clearing house items. These checks are drawn on local banks in the same community of the bank receiving them and they are assembled and presented daily to the drawee banks involved. The method of settlement is one of offset; that is, the bank sending items to the clearing house receives credit for the total of such items which in turn is offset by the total of items received in exchange. The net difference, debit or credit, is settled by draft or wire transfer depending upon the clearing house rules. The third category of items represents checks which are drawn on out-of-town banks and are often called "transit items." These checks are either collected through the Federal Reserve System or by "direct sending" to correspondents of the receiving bank.

When a check is deposited, the availability of the funds to the depositor depends upon the length of time necessary to collect the item. This, in turn, depends upon the point on which the item is drawn. If the check is an "on-us" item, the availability of funds is usually immediate as the act of collection is merely transferring a balance from one account to another in the same bank. If the check is a clearing house item, it must be presented to another local bank for payment so that funds are not available for at least a day. And, if the check is an "out-of-town" item, the period of collection may take longer than one day. While the depositing bank gives the customer provisional credit for the check when it is deposited, the availability of funds determines when the depositor may withdraw the deposit.

Each day the bank receives a large volume of items for deposit in all three of the categories mentioned. The totals of deposited items are credited to depositors' accounts and the items are sorted and processed for collection. At the same time that this is going on the depositing bank is also receiving checks which have originated in other banks under similar conditions. While some banks handle their check collections by direct sending of items to other correspondents, the majority use the facilities of the Federal Reserve System. Time does not permit us to go into this phase of banking operations, and although it is a very interesting subject, it bears only indirectly on the accounting procedures. The importance of the check collection system in so far as accounting is concerned is the matter of availability of funds. In other words, not all recorded deposits are immediately available for withdrawal since, to a certain extent, they represent items that are actually in the process of collection. This uncollected element of deposits is often referred to in the industry as "float."

Up to this point in discussing the collection of checks we have been talking about "cash items." This is a term given to checks for which provisional credit is extended during the period that the item is actually in the process of collection. If the item is not paid at the point at which it is drawn, the process is reversed and the depositor's account is charged with the return of the item. However, there are other items handled in banking as "collection items." These are given to the bank for collection but the account of the depositor or customer is not credited until collection is actually made. No accounting entries are made until the

items are paid. From the standpoint of volume these do not represent a significant number of transactions handled.

Accounting for Investment Securities

The accounting procedures for handling investment securities in the bank's portfolio are not different from those that could be anticipated in other situations. The usual procedure is that the securities are carried at cost and, if cost exceeds face, the premium is amortized against income. Some banks report income on the cash basis although many, in recognition of the fact that interest collections may be somewhat seasonal, accrue interest income on securities on a monthly basis. This is to be recommended as it records income ratably as it is earned. If it were not followed, it could lead to material distortion in the income account at interim reporting dates.

It is significant to note that, at the present time, many banks have a sizeable amount of depreciation in their bond portfolios due to bond market conditions. A few banks have established reserves, at least in part, to take care of this depreciation. However, due to the nature of the investments, the supervisory authorities have not imposed any requirement that a cost or market rule be applied to the investment security portfolio.

Legal Reserve Requirements

Some mention should be made of the legal reserve requirements in banking. "Legal reserve" refers to the amount that the bank must maintain on deposit with the Federal Reserve Bank of its district. Nonmember banks would not be covered by such a requirement, although there are certain states that have provisions in the banking law requiring certain cash reserves against deposits. The legal reserve requirement of the Federal Reserve System can act as a restraint to excessive credit since each member bank must maintain reserve balances determined by the respective percentages of demand and time deposits. These percentage requirements differ as between city and country banks.

Net Worth Accounts

All depository banking in the United States is conducted by incorporated organizations so that the net worth accounts of the bank will reflect this type of organization. Generally there are four account classifications in the net worth section. First, we have an account for capital stock. In the majority of cases only one class of stock is outstanding. During the depression years of the 1930's quite a few banks issued preferred stock, a substantial portion of which was held by the Reconstruction Finance Corporation. However, at this date substantially all of this stock has been retired and it would be the rare situation where more than one class of stock would be outstanding. Banking laws do not permit banks to issue no-par stock so that, in each instance, the capital stock account will be represented by par value shares outstanding. Also, all of the authorized stock of a bank must be subscribed and issued. There can be no authorized and unissued stock.

The second net worth account of importance is the surplus account. In banks this account is somewhat similar to paid-in surplus of other corporations and, for all practical purposes, can be considered as a part of permanent capital. The significance of the surplus account can be more

readily appreciated by the fact that the capital stock and surplus accounts together are frequently used as a yardstick in determining loan and investment limitations. For example, national banks are restricted (with certain exceptions) from making loans to any one borrower in a total amount in excess of 10% of capital and surplus accounts. The surplus account comes into existence at the time of formation of the bank. The usual requirement is that the subscribing stockholders must pay a premium over the par value of stock subscribed and a portion of this premium is credited directly to the surplus account. Thereafter annual transfers of earnings must be made until the surplus account equals the par value of outstanding capital stock.

The third net worth account for discussion is the undivided profits account. This account is the counter part to retained earnings or earned surplus of other corporations. Net earnings are periodically closed to this account and dividends and transfers to surplus are charged against it. As mentioned earlier, many banks follow the practice of closing out income and expense accounts on a semiannual basis. This is intended to facilitate the preparation of financial reports that are required by the supervisory authorities for each semiannual period.

The final net worth classification is a general one and comprises certain reserves that the bank has seen fit to appropriate out of earnings or undivided profits. These reserves are some times referred to as "after tax" reserves, since additions to them do not result in a tax benefit. Some banks have been criticized for the manner in which they use reserve accounting as a means either of leveling earnings or of disguising the extent of earnings. It is not uncommon to find transactions creating "reserves for contingencies" without any real basis for such action other than a conservative attitude on the part of the bank.

Typical Bank Records

As in all double entry accounting systems, general ledgers are the controlling records from which financial statements are prepared and also which serve to coordinate all subsidiary accounting data. The general ledger in many banks is machine-posted, and quite frequently individual entries are posted in total to the respective accounts. Certain accounts require detailed posting, however, such as accounts with correspondent banks, net worth accounts, and the like. The general ledger records of quite a few banks are so arranged that preparation of the daily statement of condition can be made directly from the trial balance of accounts.

One of the principal subsidiary records is the commercial deposit ledger. This ledger is subdivided into unit controls and each unit contains the individual checking accounts of customers. These records are machine-posted and a number of different posting plans are used; the most popular of these plans has been "dual posting." This involves duplication of posting to a separate ledger card and statement. These posting functions are performed by alternate bookkeepers. Other posting plans include single posting, "sight payment," "journal payment," etc. There are also plans that have recently been developed in conjunction with the use of electronic bookkeeping

equipment. Obviously a discussion of all of these could consume a considerable amount of time. However, for our purpose, the significant point is that there are many posting variations. Another factor that should be mentioned that would apply to any posting plan is the current practice of "deferring posting." Stated simply, deferred posting gives the bank additional time to post the accounts from the time that the items are received. Banks are required either to pay "on-us" items when received or to promptly return them to the sender. Deferred posting gives the bank the opportunity of an additional grace period in which to process the items. The control account totals are posted ahead of the detailed posting to the accounts.

Separate depositor ledgers are maintained for savings accounts. These are often machine-posted and are subdivided in the same manner as the checking accounts. Savings accounts are usually arranged in numerical order whereas checking accounts are alphabetical. Posting procedures for savings accounts may be on either the "unit plan" or the "dual plan." The unit plan involves simultaneous posting of the customer's passbook and ledger card by the teller when the transaction takes place. Special accounting equipment is used for this purpose and has various control features to insure the proper handling and recording of transactions. The dual plan separates the teller and bookkeeping functions so that they are performed by different employees. Again, we could spend a lot of time talking about procedural aspects, however, for the present, the foregoing will suffice to give a general idea of the records used in the savings department.

Another subsidiary record commonly used in the banking industry and one that should be mentioned is the "liability ledger." This is somewhat of a misnomer as it is a record used to record the indebtedness of borrowers which, of course, is an asset to the bank. This record is sometimes hand-posted, although many banks, in recognition of the added control features, have converted it to machine-posting. The liability ledger is in a sense a memorandum record. The loan control accounts are supported by notes and in many cases there will be more than one obligation of a single borrower. Moreover, the notes are frequently filed in maturity date order. The function of the liability ledger is to reclassify the indebtedness by borrower so that his total liability to the bank can be ascertained.

There are many other subsidiary records used to summarize details controlled through general ledger accounts. For example, the general ledger contains liability accounts for outstanding official obligations such as cashier's checks, certificates of deposit, dividend checks, etc. Registers must be maintained to supply information on the individual items as to each of these classifications. There are also accounts that are maintained with correspondent banks. In some cases these are carried in the general ledger, however, where any appreciable volume of accounts is involved, they are maintained in subsidiary ledgers.

One more word about the typical accounting records of a bank. As was mentioned earlier, there is a continuing need for speed in classifying and summarizing accounting transactions. This dictates a certain degree of expediency in the accounting processes. You will find that accounting infor-

mation is often abbreviated or held to a bare minimum. Some banks might be considered deficient by our standards in failing to provide adequate explanations of transactions. However, it is usually possible to analyze the accounts, although in some instances you will find that, in order to do this, you may have to refer to several records and to the supporting data to obtain all the information required.